(1) Supreme Court, U.S.
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IN THE

Supreme Court of the United States

LORRAINE GRACE, individually and as Executrix of the Estate of OLIVER R. GRACE, GERALD I. WHITE, As Executor of the Estate of MORGAN H. GRACE, and GERALD I. WHITE, Trustee of the John E. GRACE TRUST, individually and as stockholders of BRIGGS LEASING CORPORATION suing on behalf of themselves and for the benefit of said corporation and for the class of other stockholders of said corporation similarly situated,

Petitioners,

against

ROBERT GENSER,

Respondent,

and

ROBERT ROSENSTOCK, EDWARD ROSENSTOCK, BRIGGS LEASING CORPORATION and BRIGGS ACQUISITION CORPORATION,

Defendants.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

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Questions Presented

1. Where the facts here conclusively establish a Rule 10b – 5 cause of action under the holding in *Sante Fe v. Green*, 430 U.S. 462 (1977), did the lower courts err as a matter of law in overlooking such controlling precedent?

2. Did the lower courts err as a matter of law in applying a holding on "causation" under Rule 14a–9 which addressed limited concerns for proxy solicitation to eliminate a claim under Rule 10b–5 for deception, fraud, fiduciary breach and scienter?

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Petition For A Writ Of Certiorari To The United States Court Of Appeals For The Second Circuit

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Petitioners respectfully petition for a Writ of Certiorari to review part of the judgment of the Second Circuit Court of Appeals in this case.

OPINIONS BELOW

The Second Circuit opinion in this class action affirming, *inter alia*, the dismissal of the amended complaint against defendant, Robert Genser, after a bench trial, as a matter of law, without any findings of fact, for alleged violations of §10(b) of the Securities Exchange Act of 1934 ("1934 Act") and Rule 10b-5 promulgated thereunder by the Securities and Exchange Commission (1a) is reported at *Grace v. Rosenstock*, 228 F.3d 40 (2d Cir. 2000). The Memorandum and Order in the United States District Court for the Eastern District of New York, Robert M. Levy, Magistrate Judge, (51a) is reported at *Grace v. Rosenstock*, 23 F. Supp. 2d 326 (1998).

STATEMENT OF JURISDICTION

The jurisdiction of this Court is invoked under 28 U.S.C. §1254(1).

The judgment of the Second Circuit Court of Appeals was entered on August 25, 2000. The Court of Appeals entered an order denying a timely petition for rehearing and declining a petition for rehearing en banc on October 26, 2000 (46a-47a).

On August 15, 1997, as a result of a settlement, the District Court entered a judgment in favor of the plaintiffs class against defendant Robert Rosenstock in the amount of $6.9 million and against defendant Briggs Leasing Corporation in the amount of $4 million (48a-50a). The action against defendant Robert Genser ("Genser") was severed. The appraisal action by plaintiffs in the New York State Supreme against Briggs Leasing Corporation to fix the fair value of plaintiffs' shares as dissenting shareholders under Section 623 of the Business Corporation Law was rendered moot (id).

After trial against defendant Genser, the District Court by Magistrate Judge Robert M. Levy, *sua sponte* dismissed the §10(b) and Rule 10(b)5 claims, as a matter of law, under the authority of *Virginia Bankshares, Inc. v. Sandberg*, 501 U.S. 1083, 111 S. Ct. 2749, 115 L. Ed. 2d 929 (1991), without making any findings of fact. Thus, this litigation is now ripe for review by this Court inasmuch as there is a final judgment that has disposed of all the claims of the amended complaint against all the parties.

STATUTES AND RULES INVOLVED

Section 10(b) of the 1934 Act, in pertinent part, provides:

> It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce or of the mails, or of any facility of any national securities exchange –
>
> * * * *
>
> (b) To use or employ, in connection with the purchase or sale of any security registered on a national securities exchange or any security not so registered, any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the [Securities and Exchange] Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.

The Securities and Exchange Commission has adopted Rule 10b-5, pursuant to its §10(b)

rulemaking authority, which, as relevant here, provides:

> It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails or of any facility of any national securities exchange,
>
> (a) To employ any device, scheme, or artifice to defraud, [or]
>
> * * * *
>
> (c) To engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person, in connection with the purchase or sale of any security.

Section 14(a) of the 1934 Act provides:

> [it] shall be unlawful for any person, by the use of the mails or by any means or instrumentality of interstate commerce or of any facility of a national securities exchange or otherwise, in contravention

> of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors, to solicit or to permit the use of his name to solicit any proxy or consent or authorization in respect of any security (other than an exempted security) registered pursuant to section 781 of this title.

Rule 14a-9 promulgated by the Securities and Exchange Commission provides in relevant part that:

> [no] solicitation subject to this regulation shall be made by means of any proxy statement . . . containing any statement which, at the time and in the light of the circumstances under which it is made, is false or misleading with respect to any material fact, or which omits to state any material fact necessary in order to make the statements therein not false or misleading. . . .

17 C.F.R. §240.14a-19(a) 1999.

STATEMENT

Petitioners, minority shareholders of Briggs Leasing Corp. ("Briggs"), brought this civil, class action as a result of a cash out merger in 1985 with no business

purpose. Defendants Robert Rosenstock ("Rosenstock") and Genser were directors and owned 72% of Briggs' outstanding common stock which assured approval of the merger, irrespective of the vote of the minority shares. Rosenstock's father, Edward, was the other director. The claims in the amended complaint were for material misrepresentations and omissions of material facts in the Proxy Statement and fraud in the merger in violation of §10(b) and Rule 10b-5 of the 1934 Act and the state claims of breach of fiduciary duty of loyalty and unjust enrichment where the majority stockholders and directors in a self interested deal froze out the minority at a unilaterally determined and grossly unfair price of $1.50 per share, for a total value of Briggs of $894,000 ($1.50 multiplied by all of the 595,728 outstanding shares). At trial plaintiffs' expert testified that the value of the real estate on the merger date was $2.5 million or 500% greater than that assigned to it (105a-106a). Defendants failed to offer any expert testimony in rebuttal and none was included in the Proxy Statement. Thirty-two months after the merger, Briggs' real estate was appraised at $4.8 million, or almost 1000% above the merger price. During the years 1986, 1988 and 1989, Briggs issued mortgages of $10.6 million on its only real estate property, but Briggs received only $2 million and over $8.6 million was diverted to and deposited directly into Robert Rosenstock's personal bank account or was paid to third parties for obligations

of ventures controlled by defendants Rosenstock and Genser.

REASONS FOR GRANTING THE WRIT

THE COURTS BELOW OVERLOOKED THE CONTROLLING AUTHORITY OF THIS COURT'S DECISION IN *SANTA FE V. GREEN.*

Santa Fe Industries, Inc. v. Green, 430 U.S. 462 (1977) held that a cause of action under §10(b) or Rule 10b-5 requires at least deception or manipulation in order to trigger the application of fraud and fiduciary breach under §10(b) or Rule 10b-5(a) or (c). The Court held (*id.* at 473-474*)*:

> Thus the claim of fraud and fiduciary breach in this complaint states a cause of action under **any part of Rule 10b-5** only if the conduct alleged can be fairly viewed as "manipulative or deceptive" within the meaning of the statute.

Inasmuch as there was full disclosure of all the material facts in *Santa Fe* there was no deceptive or manipulative conduct. But here, misrepresentations and nondisclosure in the proxy statement provide the necessary deception (10a). Other critical facts in *Santa Fe* that are important to the case at bar are:

Santa Fe, owning, 95% of its subsidiary, used Delaware's short form freeze out merger statute – which only required a resolution of Santa Fe's Board of Directors to approve the merger – to force the minority shareholders in the subsidiary to sell all their shares to Santa Fe; the day after the merger the shareholders were advised by an Information Statement that their shares had been sold the day before to Santa Fe at $150 per share and the appraised value of the physical assets was $640 per share and if the minority disagreed with the price, they had dissenter's rights for an appraisal under Delaware law. The minority shareholders were not given advance notice of the merger and the statute also did not require their consent or an opportunity to vote; **in short, the minority had no vote in the merger approval process.**

Our case meets each and every requirement of the holding in *Santa Fe*. The Courts below here assumed deception through misrepresentations and nondisclosures in the proxy statement (10a). The freezeout here was accomplished through a long form merger. Because the majority stockholders owned 72% of the stock, the merger was assured irrespective of the minority's vote. Like in *Santa Fe*, the vote of the minority shareholders **was not necessary** to approve the merger. For purposes of the merger, Briggs' real estate, its principal asset, was valued at $500,000 when its actual unrefuted value was 500% higher at $2.5 million (105a –

106a). The cause of action here – like in *Santa Fe* – was for fraud and breach of fiduciary duty under Rule 10b-5(a) or (c) by forcing the minority to sell their shares at a grossly, unfair price of $1.50 per share. Also like in *Santa Fe*, shareholders were given dissenter's rights to an appraisal under New York law.

Plaintiffs here have the deception that was absent in *Santa Fe*. Under those circumstances, the facts here fall squarely within a cause of action under §10(b) and Rule 10b-5 under *Santa Fe's* **holding.**

This Court in *Santa Fe* did not reverse the holding of **causation** as found in *Green v. Santa Fe Industries, Inc.* in the Second Circuit, 533 F. 2d 1283, 1287 (2d Cir. 1976):

> Without further discussion we think it is clear that the case relates to the purchase and sale of securities in interstate commerce[3], that the plaintiffs are indeed forced sellers[4], and **that there is a causal relation** between the alleged breach of fiduciary duty by the majority and the injury suffered by the

complaining owners of the minority stock interest.

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3. *Vine v. Beneficial Finance Co.*, 374 F.2d 627, 634 (2d Cir.), cert. denied, 389 U.S. 970, 88 S.Ct. 463, 19 L.Ed.2d 460 (1967); *Popkin v. Bishop*, 464 F.2d 714, 718 n. 8 (2d Cir. 1972).

4. *Vine v. Beneficial Finance Co.*, supra, at 635.

Causation was so clear and obvious in *Santa Fe*, that this Court accepted the Second Circuit's analysis. Indeed, in *Santa Fe*, the minority had no say whatsoever in either a vote or consent as to their sale of all their shares. The minority did absolutely nothing in *Santa Fe*. Clearly, it was the *Santa Fe* Board of Director's resolution that caused the minority shareholders to sell all their shares to the majority and thereby eliminate the minority at an unfair price. A clearer case of causation, transaction and loss, would be hard to find. Likewise here, the vote given to the minority was meaningless where majority approval of the merger was guaranteed by reason of their percentage ownership. Accordingly, as in *Santa Fe*, causation is clear and beyond all doubt.

A. The Nature Of The Forced Sale Establishes Causation; In Any Event, Petitioners Proved Both Loss And Transaction Causation

In *Vine v. Beneficial Finance Co.*, 374 F.2d at 635, the Second Circuit, regarding the requirement of a plaintiff to show reliance in a freeze out merger where the minority vote is not allowed or not necessary in a Rule 10b-5 action, held:

> Whatever need there may be to show reliance **in other situations** ... we regard it as **unnecessary** in the limited instance when no volitional act is required and the **result of a forced sale** is exactly that intended by the wrongdoer. Since the complaint alleges that plaintiff, in effect, has been forced to divest himself of his stock and this is what defendants conspired to do, reliance by plaintiff on the claimed deception need not be shown.

In sum, the Second Circuit held that "reliance by the plaintiff on the claimed deception need not be shown" because the minority – not allowed a vote in the short form merger – was forced by the wrongdoer to sell his shares and no volitional act was required of such plaintiff minority shareholder.

Thus, the *Vine* Court was perfectly clear that it is unnecessary to show reliance when "no volitional act is required" by the minority and "the result of a forced sale is exactly that intended by the wrongdoer" (*Vine*, at 635). That *Vine* holding applies squarely to the freeze out merger part of the transaction; there was no need for the *Vine* plaintiff to show reliance by him on the deception committed against other class A stockholders previously cashed out by a tender offer by the wrongdoer. The Second Circuit's reasoning as to why the case at bar is distinguishable from *Vine* is erroneous. The Court pointed out that in *Vine* there was this two-phase scheme to eliminate Class A shareholders and deception must be shown which caused their injury and the allegation in *Vine* met that test. The Court contrasts the case at bar by stating "there is no suggestion that [petitioners] acquired those share by means of fraud." But that is not what the reliance and causation language refers to concerning the forced sale. That deception committed in the tender offer – not the short form merger – did not relate to plaintiff who did not sell at the time, that deception permitted the wrongdoer to acquire 95% of the stock so it could then, through the device of the short form merger, make plaintiff a forced seller. The *Vine* Court treated the deceptive tender offer and the fraudulent forced sale through the freeze out merger as one transaction for purposes of its Rule 10 b – 5 analysis. But plainly plaintiff did not have to show reliance on his forced sale of his shares.

The fact that the deception was utilized by the wrongdoer initially to acquire its 95% of the stock in *Vine* , does not mean that it is the only way one may show deception under Rule 10 b – 5. Indeed, plaintiffs here established deception through non-disclosures and misrepresentations in the proxy statement. Accordingly, the Second Circuit's statement that Rosenstock and Genser did not acquire their controlling ownership of shares "by means of fraud" is irrelevant and is not a substantive distinction (24 a).

Significantly, the Ninth Circuit agrees with plaintiff's reading of *Vine*. In *Jacobson v. AEG Capital Corp.*, 50 F.3d 1493 (9th Cir. 1995), the Ninth Circuit held:

> A shareholder who is forced to sell or alter her securities as the result of a fraudulent scheme is deemed a seller for purposes of the securities laws. The forced sale doctrine also eliminates the reliance requirement. Since a fraudulent scheme forced the sale or alteration of securities, a shareholder bringing an action under the forced sale doctrine need not prove reliance because she made no investment decision to participate in the transaction – the sale was forced by the operation of some rule (e.g., a short-form merger). Vine, 374

> F.2d at 635 ("Whatever need there may be to show reliance in other situations ... we regard it as unnecessary in the limited instance when no volitional act is required and the result of a forced sale is exactly that intended by the wrongdoer").

Accordingly, the *Grace* case has caused a serious split in the Circuits as to how a forced sale affects the reliance and causation requirement in a 10b-5 action.

In any event, a factual analysis demonstrates that plaintiffs here proved the two elements of causation: transaction causation and loss causation. The Second Circuit in an extensive analysis of causation in *AUSA Life Insurance Company v. Ernst and Young*, 206 F.3d, 202, 209 (2d Cir. 2000) held:

> Loss causation is causation in the traditional "proximate cause" sense -- the allegedly unlawful conduct caused the economic harm. ...Transaction causation means "the violations in question caused the appellant to engage in the transaction in question." ... Transaction causation has been analogized to reliance.

Here, both are easily established. Loss causation consists of the unlawful conduct – deception, fraud

and breach of fiduciary duty – which is the forced sale due to the majority's share ownership at a grossly unfair price through a deceptive proxy statement, where a vote by the minority was not necessary. That conduct plainly caused economic harm to the minority shareholders. The deception, the securities transaction, the fraud, the breach of fiduciary duty and the economic loss thus coincide. Clearly, the majority's unlawful conduct caused the economic harm to the plaintiffs class by forcing them to sell their shares at the unconscionable price of $1.50 per share. As held in *AUSA,* the damage complained of is required to be a "foreseeable" consequence of the fraud, fiduciary breach and deception. Certainly here the economic harm to the minority was foreseeable by the majority (*id* at 212, 217). Clearly, the majority's violations spelled out above, were the proximate cause of plaintiffs class' economic harm.

Transaction causation requires that the "violations in question" caused the plaintiffs to engage in the transaction. That is also clear here. The majority shareholders breached their fiduciary duty by using their controlling shares to force the minority to sell their shares to the majority at a fraudulently low price. Plainly, the majority's violations caused the plaintiffs to engage in the transaction. The minority, like in *Santa Fe,* had no choice, but to forcibly sell their shares (*id.* 209-210).

Accordingly, there was both transaction causation and loss causation. Respectfully, the following holding of the Second Circuit defies logic and common sense (25a):

> Plaintiffs here, because minority shareholder votes were not required for approval of the merger that was the subject of the proxy statements, did not show causation based on the approval of the merger.

The focus of the causation for the approval of the merger must be on the majority shareholders with the power -- through their percentage ownership of shares -- to force the transaction on the minority shareholders inasmuch as the minority votes are either not allowed -- as in a short form merger in *Santa Fe* or *Vine* -- or not necessary to approve the merger – as is the case here. As the Court stated in *Vine*, it is more appropriate to refer to the transaction as a forced purchase since the majority shareholder purchaser is the wrongdoer, 374 F.2d at 635.

Accordingly, the Court of Appeals erred because petitioners did establish causation based on the majority's approval of the merger.

Virginia Bankshares' held that where the majority has sufficient votes to approve a transaction then there is no causation under §14(a)

or Rule 14a-9 even if the Proxy Statement is false and misleading. The Second Circuit cited that holding and then erroneously held that the holding in *Virginia Bankshares* also applies to claims of deception in a Proxy Statement under §10(b) and Rule 10b-5 and a "plaintiff may not recover on such a claim without proving that his injury was caused by the fraud [deception]" (25a). The Second Circuit is actually applying the holding of *Virginia Bankshares* under Rule 14a-9 to deceptive proxy statements under Rule 10b-5 as though there was no fraud or fiduciary breach covered by Rule 10b-5(a) or (c). But once fraud and fiduciary breach are recognized as part of Rule 10b-5(a) or (c), then that demonstrates the error in the Second Circuit's automatically applying the holding of *Virginia Bankshares* on causation under Rule 14a-9 to ~~eradicate~~ fraud and fiduciary breach under Rule 10b-5(a) or (c) as though Rule 14a-9 and Rule 10b-5 address the same standard of liability.

This Court in *Herman & MacLean v. Huddleston,* 459 U.S. 371 382 (1983) held Rule 10b-5 (i) is a "catch-all" antifraud provision that "requires a plaintiff to carry a [heavy] burden to establish a cause of action" (*id.* at 382), (ii) which can be "brought by a purchaser or seller of '**any** security' against '**any** person' who has used '**any** manipulative, or deceptive devise or contrivance' in connection with the purchase or sale of a security" (*id.)* (original emphasis), and (iii) which requires

proof that "defendant acted with scienter, *i.e.*, with intent to deceive, manipulate, or defraud" (*id.*)

The Court in Herman & MacLean, stated that the existence of this implied remedy [under §10(b) and Rule 10b-5] is simply beyond peradventure" and "has been consistently recognized for more than 35 years", 459 U.S. at 380.

Thus, even though the allegedly fraudulent conduct expressly provides the basis for damages under §11 of the 1933 Act, that does not bar the "established [implied] remedy for fraud" under the 1934 Act (id. at 381). Most significantly, this Court stated that the "resolution of this issue turns on the fact that the two provisions involve distinct causes of action, and even intended to address different types of wrongdoing" (id). The same is true as to Rule 10b-5 and Rule 14a-9.

This Court held that because §11 and §10(b) address different types of wrongdoing, there is **"no reason to carve out an exception to §10(b) for fraud occurring in a registration statement just because the same conduct may also be actionable under §11"** (*id.*) at 382-383). This Court further held that to exempt "such conduct from liability under §10(b) would conflict with the basic purpose of the 1933 Act: to provide greater protection to purchasers of registered securities. It would be

anomalous indeed if the special protection afforded to purchasers in a registered offering by the 1933 Act were deemed to deprive such purchasers of the protections against manipulation and deception that §10(b) makes available to all persons who deal in securities" (*id.* at 383). Likewise, here, forced sellers should not be deprived of use of Rule 10b-5 for deception and fraud because of the holding in *Virginia Bankshares* on Rule 14a-9.

This Court further stated that the "1934 Act and the 1933 Act 'prohibit some of the same conduct" and "some overlap is neither unusual nor unfortunate" (*id.*). This Court also noted that §28(a) of the 1934 Act contains a savings provision parallel to §16 of the 1933 act that unequivocally states that "[t] he rights and remedies provided by this title shall be in addition to any and all other rights remedies that may exist at law or in equity" (*id*). It further emphasized that these "provisions confirm that the remedies in each Act were to be **supplemented by 'any and all' additional remedies"** (id.).

This Court further held in *Herman & MacLean*, 459 U.S. at 384-387:

> This cumulative construction of the remedies under the 1933 and 1934 Acts is also supported by the fact that, when Congress comprehensively revised the

securities laws in 1975, a consistent line of judicial decisions had permitted plaintiffs to sue under §10(b) regardless of the availability of express remedies. In 1975, Congress enacted the

> most substantial and significant revision of this country's Federal securities laws since the passage of the Securities Exchange Act in 1934.

... In light of this well-established judicial interpretation, Congress' decision to leave §10(b) intact suggests that Congress ratified the cumulative nature of the §10(b) action.

* * * *

The effectiveness of the broad proscription against fraud in §10(b) would be undermined if its scope were restricted by the existence of an express remedy under §11. Yet we have repeatedly recognized that securities laws combating fraud should be construed "not technically and restrictively, but flexibly to effectuate [their] remedial purposes." [citations omitted]. **We therefore reject an interpretation of the securities laws that displaces an action under §10(b).**

By applying the Virginia Bankshares ruling under §14(a) relating to the vote of the minority being unnecessary to approve the transaction to §10(b) without any analysis of the purpose of §10(b), the Courts below effectively displaced §10(b) in contravention of this Court's binding authorities.

In *Mills v. Electric Auto-Lite Co., 396 U.S. 375, 384 (1970),* decided under §14(a) and Rule 14a-9, the Court held that where there is a material misstatement or omission in a proxy statement, "the defect was of such a character that it might have been considered important by a reasonable shareholder who was in the process of deciding how to vote." The Court further held (*id.384*) that a shareholder must make a "sufficient showing of a causal relationship between the violation and the injury for which he seeks redress, if, as here, he proves that the **proxy solicitation itself**, rather than the particular defect in the solicitation materials, was an essential link in the accomplishment of the transaction". *Virginia Bankshares* held that inasmuch as the minority shareholders' vote was not necessary to approve the transaction, then the "proxy solicitation itself" was **not** "an essential link in the accomplishment of the transaction." (*id.385*). Thus, the minority shareholder could not show any causal connection between the wrong and his injury. Therefore, there could not be any injury to a minority shareholder in deciding whether to vote for

or against the transaction where the shareholder vote did not count.

> Therefore, the Second Circuit erred in the following critical holding (25a):
>
> > Plaintiffs here, because minority shareholders votes were not required for approval of the merger that was the subject of the proxy statements, did not show causation based on the approval of the merger.

Put simply, *Virginia Bankshares* did not overrule *Santa Fe v. Green*. *Santa Fe* is still the law and plaintiffs met all of its requirements for a cause of action under §10(b) and Rule 10b-5. Santa *Fe* recently cited by this Court with approval in *United States v. O'Hagan*, 521 U.S. 642, 655 (1997), demonstrates that it is still controlling authority on Rule 10b-5.

Despite petitioners' heavy reliance on *Santa Fe*, **the lower courts failed to even cite or discuss** *Santa Fe*. The doctrine of *stare decisis* required the courts below to follow *Santa Fe*. Instead, the lower courts committed gross error in overruling *Santa Fe sub silento*. By not following *Santa Fe*, the decisions below were built on an erroneous premise and the rationale that followed was a non-sequitor.

B. The Lower Courts Erred In Applying *Virginia Bankshares* Relating to False and Misleading Proxy Statements Under Rule 14a-9 To Eliminate Rule 10b-5 Claims Based on Deception under §10(b) and Fraud and Fiduciary Breach under Rule 10b-5(a) or (c)

In their analysis, the lower courts overlooked the fraud and fiduciary breach that plaintiffs proved here under Rule 10b-5(a) or (c). Thus the courts below erred by treating Rule 10b-5 as though it only covered deception (Rule 10b-5(b)) in connection with the purchase or sale of a security and then treated the entire Rule 10b-5 as though it covered the "same concerns" as Rule 14a-9 (22a). However, as demonstrated above, Rule 10b-5 covers deception plus fraud under Rule 10b-5(a) or (c). Accordingly, the Second Circuit's failure to discuss the "fraud" branch of Rule 10b-5 (a) or (c) undercuts its treatment of Rule 10b-5 as a twin of Rule 14a-9.

The Second Circuit held that inasmuch as *Virginia Bankshares* only addressed proxy claims under §14(a) and Rule 14a-9,

> its express reliance on the rationale of *Blue Chip Stamps*, a case involving §10(b) and Rule 10b-5, demonstrates that the same concerns compel the

> conclusion that the scope of the implied private right of action under either set of provisions does not encompass claims based on "a merely hypothetical ... set of facts that never occurred." *Virginia Bankshares*, 501 U.S. at 1105.

(22a-23a). However, the Supreme Court in *Blue Chip Stamps* held that §10(b) and Rule 10b-5 did not apply because the plaintiffs were not buyers or sellers of securities. Thus, it was a case that did not even trigger the application of §10(b) and Rule 10b-5. Indeed, the concerns expressed in *Blue Chip Stamps* related to "what a merely hypothetical buyer or seller might have done on a set of facts that never occurred and foresaw that any such expanded liability would turn on 'hazy' issues ... inviting ... strike suits ... with little chance of reasonable resolution ... These were good reasons to deny recognition to such claims..." (21a). In short, Blue Chip set forth the dangers of allowing a claim under Rule 10b-5 where there was only a "hypothetical buyer or seller" and what he "might have done on a set of facts that never occurred." But here there is no such danger. We are dealing with actual, not hypothetical, sellers and we are dealing with facts that did occur. Thus, the concerns set forth in Blue Chip are wholly absent here under Rule 10b-5 and §10(b) where fraud and fiduciary breach did occur – as well as deception – which Santa Fe held is actionable.

CAUSATION HERE IS ALSO ESTABLISHED BECAUSE PLAINTIFFS' FORFEITED THEIR STATE REMEDY

"The *Virginia Bankshares* Court left open the possibility that even minority shareholders whose votes were not necessary for approval of the proposed merger might nonetheless satisfy the causation requirements if they could show that the violations induced them to forfeit a state remedy" (25a).

Here, the Second Circuit upheld forfeiture of a state remedy as a means of establishing causation. *Wilson v. Great American Indus. Inc.*, 979 F.2d 924 (2d. Cir. 1992); *Goldberg v. Meridor*, 567 F.2d 209, 219 (2d Cir 1977), *cert. denied*, 434 U.S. 1069 (1978). The Court below stated that: "under New York law governing freeze-out mergers, except for an 'appropriate' equitable action as envisioned by BCL §623(k) appraisal is the dissenting shareholders' exclusive remedy" (27a). The Court held that plaintiffs did not forfeit a state law remedy because their appraisal suit was rendered moot pursuant to a stipulation and although District Court Judge Costantino, by a 1986 order characterized plaintiff's claim as requests for **equitable** relief, the Second Circuit said the order is interlocutory and therefore subject to modification. (29a-30a). The Court further claimed the posture of the case changed at the time of trial because plaintiff had

settled their claims against Briggs and could no longer seek the equitable claim of recission and further, no remaining derivative claims existed. (30a). Plaintiff submits that once it brought an equitable action, the determination of whether plaintiff forfeited its state remedy to determine causation did not change every time a defendant was settled out. The fact is the action was equitable in nature **at the time** causation was established, and plaintiff forfeited their state law remedy then – at the time of the freeze-out – not at the time of the 1998 trial.

Furthermore, the deceptive proxy statement and the fraudulent merger and fiduciary breach caused the injury because the minority shareholders could have sought an injunction under New York law had the defendants not lulled the minority shareholders into security by the deceptive disclosure.

THE SPLIT IN THE CIRCUITS SHOULD BE RESOLVED

The Second Circuit's automatic application of the Rule 14a-9 holding in *Virginia Bankshares* to Rule 10b–5 involving deception and fraud has resulted in a split in the Courts of Appeals. The Third Circuit in *Scattergood v. Perelman*, 945 F. 2d 618 (3d Cir. 1991) appears to be aligned with the Second Circuit's decision here. The Sixth Circuit in

Howing Company v. Nationwide Corporation, 972 F. 2d 700 (6th Cir. 1992) held that "nonvoting theories of causation can support a §13(e) claim, [and] minority shareholders with insufficient votes to block a transaction have protection" (*id.* at 706). Thus, the Sixth Circuit did not read *Virginia Bankshares* as broadly as the Second and Third Circuits. It is also noteworthy that the Second Circuit in *Wilson v. Great American Industries, Inc.*, 979 F. 2d 924 (2d Cir. 1992) involving Rule 14 a – 9 held that *Virginia Bankshares* "did not hold that minority shareholders whose votes number too few to affect the outcome of a shareholder vote may never recover damages under §14(a), and directed that the District Court could still consider the §10 (b) and Rule 10b–5 claims not previously ruled upon by the Second Circuit. It is most important that Rule 10b–5 as a major enforcement vehicle in private litigations not be subverted by the holding of the Second Circuit below, otherwise the full disclosure purpose of Rule 10b–5, and the prevention of fraud and deception will be undermined.

CONCLUSION

The petition for a writ of certiorari should be granted.

Dated: January 24, 2001

Respectfully submitted,
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APPENDIX A

United States Court of Appeals,
Second Circuit.

(Argued: Nov. 19, 1999 Decided: Aug. 25, 2000)
Docket No. 98-9618.

Lorraine GRACE, Individually and as Executrix of the Estate of Oliver R.Grace, Gerald I. White, As Executor of the Estate of Morgan H. Grace, and Gerald I. White, Trustee of the John E. Grace Trust, individually, and as stockholders of Briggs Leasing Corporation, suing on behalf of themselves and for the benefit of said corporation and for the class of all other stockholders of said corporation similarly situated,

Plaintiffs-Appellants,

— v.—

Robert ROSENSTOCK, Edward Rosenstock, Briggs Leasing Corporation and Briggs Acquisition Corporation,

Defendants,

Robert GENSER,

Defendant-Appellee.

Bank Leumi Trust Company Of New York, David Mack, Leo V. Berger, Apex Marine Corporation and Gary Holman,

Proposed Defendants-Appellees.

Before:

KEARSE, PARKER, and POOLER,
Circuit Judges.

Appeal from a judgment of the United States District Court for the Eastern District of New York, Robert M. Levy, *Magistrate Judge*, dismissing claims against defendant-appellee under Securities Exchange Act of 1934 and state law in connection with freeze-out merger, *see* 23 F.Supp. 2d 326 (1998), and denying leave to file a supplemental complaint against persons not previously named as defendants.

Affirmed.

Sidney Bender, New York, New York (Risa Bender, Leventritt Lewittes & Bender, New York, New York, on the brief), for Plaintiffs- Appellants.

Herbert Rubin, New York, New York (David B. Hamm, Miriam Skolnik, Herzfeld & Rubin, New

York, New York, on the brief), for Defendant-Appellee.

Robert Fryd, New York, New York (Donald M. Levinsohn, Warshaw Burstein Cohen Schlesinger & Kuh, New York, New York, on the brief), for Proposed Defendant-Appellee Bank Leumi Trust Company.

Andrew J. Entwistle, New York, New York (William S. Gyves, Entwistle & Cappucci, New York, New York, on the brief), for Proposed Defendants-Appellees Berger, Mack, and Apex Marine Corporation.

David K. Bergman, New York, New York (Fred M. Weiler, Siller Wilk, New York, New York, on the brief), for Proposed Defendant-Appellee Holman.

KEARSE, Circuit Judge:

Plaintiffs Lorraine Grace et al., individually and representing former stockholders of defendant Briggs Leasing Corporation ("Briggs"), appeal from a judgment of the United States District Court for the Eastern District of New York, Robert M. Levy, Magistrate Judge, dismissing their amended complaint against defendant Robert Genser for alleged violations of §10(b) of the Securities Exchange Act of 1934 ("1934 Act"), 15 U.S.C. §78j(b) (1994), Rule 10b-5 promulgated thereunder by the Securities and Exchange Commission

("SEC" or "Commission"), 17 C.F.R. §240.10b-5 (1999), and New York law, in connection with the 1985 freeze-out merger of Briggs and defendant Briggs Acquisition Corp. ("BAC"). The district court, following a bench trial, dismissed the §10(b) and Rule 10b-5 claims on the ground that plaintiffs had failed as a matter of law to prove causation; the court dismissed plaintiffs' state-law claims on the ground that appraisal under N.Y. Bus. Corp. L. §623 (McKinney 1986) was their exclusive remedy. *See* 23 F.Supp.2d 326 (1998). On appeal, plaintiffs contend principally that they were not required to prove causation, and that if required to do so they met their burden. Plaintiffs also challenge an interlocutory order denying their motion for leave to file a second-amended and supplemental complaint asserting new state-law claims against Genser and several proposed new defendants. For the reasons that follow, we affirm.

I. BACKGROUND

Prior to 1985, Briggs was a publicly-held auto-leasing company incorporated in New York. Defendants Robert Rosenstock ("Rosenstock"), his father Edward Rosenstock, and Genser were officers and directors of Briggs and owned, respectively, approximately 64%, 3%, and 5% of its outstanding stock.

Plaintiffs Lorraine Grace and Gerald I. White, individually or as trustees or executors, are or represent former stockholders of Briggs who owned a total of 7,476 shares of Briggs, or approximately 1.25% of its outstanding stock.

In early 1985, Rosenstock and Genser decided to take Briggs private in a freeze-out merger. Accordingly, they incorporated BAC, planning to merge BAC and Briggs, buy out Briggs's minority shareholders, and make Briggs the surviving corporation. Rosenstock and Genser contributed all of their Briggs shares to BAC; Rosenstock also purchased his father's shares and contributed those to BAC. As a result, BAC owned 72% of the stock of Briggs, with Rosenstock and Genser owning all of the stock of BAC. Under New York's Business Corporation Law ("BCL"), a merger may be authorized by the affirmative vote of two-thirds of the corporation's shares. *See* N.Y. Bus. Corp. L. §903(a)(2) (McKinney Supp.1999).

In January 1985, Briggs sent its shareholders notice of, and a proxy statement for, a special meeting to vote on the proposed merger. The notice informed shareholders, *inter alia*, that (a) because BAC owned 72% of Briggs's shares and would vote those shares in favor of the merger, approval was assured irrespective of the votes of Briggs's other shareholders; (b) all minority shareholders would be forced to sell their shares to the surviving

corporation for $1.50 per share; (c) after the merger, the BAC shares would be converted to shares of Briggs; and (d) Rosenstock and Genser, who owned all of the shares of BAC, would thus become the sole shareholders of Briggs. The proxy statement ("Briggs proxy statement" or "proxy statement") also stated that dissenting shareholders would have the right under New York law to obtain an appraisal of, and payment for, the fair value of their shares.

At the meeting, plaintiffs voted their shares against the merger, which was approved based on BAC's vote. The merger was consummated on February 26, 1985, and Rosenstock and Genser became the sole holders of Briggs shares, owning approximately 93% and 7%, respectively.

A. *The Present Action: The First Twelve Years*

Plaintiffs commenced the present action in June 1985 as an individual, derivative, and class action, requesting equitable and monetary relief against Briggs, BAC, Rosenstock, Edward Rosenstock, and Genser; the amended complaint was filed a month later. Contemporaneously, plaintiffs sued in New York state court, asserting appraisal rights under BCL §623; proceedings in that suit were stayed pending disposition of this action.

The amended complaint in the present action alleged principally that the Briggs proxy statement was false and misleading by reason of numerous material omissions and untrue statements, including vast understatements of the compensation paid by Briggs to Rosenstock, Edward Rosenstock, and Genser; false representations that the reason for the merger was to relieve Rosenstock and Genser of their roles as personal guarantors of Briggs's debt, when in fact the primary guarantor of such debt until January 1985 was Charlotte Rosenstock (Rosenstock's mother) and the entrance of Rosenstock and Genser as guarantors was spuriously devised to provide a facially valid reason for the merger; and the false valuation of Briggs's real estate at $883,503, when in fact its value exceeded $2 million.

The amended complaint also alleged that the Briggs proxy statement failed to disclose, *inter alia*, that Rosenstock and Genser pursued the merger as part of a scheme to divert the assets of Briggs to themselves; that they had plans to develop certain of Briggs's real estate into an office-building-supermarket complex for their own benefit; that a third party had offered in excess of $1.5 million for Briggs's real estate; that in January 1985 a third party had offered $3.00 per share for Briggs stock; and that Briggs assets had been diverted to defendants' personal use to fund the individual defendants' opulent lifestyles.

The amended complaint asserted that defendants' conduct violated §10(b) and Rule 10b-5, as well as various provisions of New York common law and statutory law dealing principally with securities fraud and shareholders meetings. Invoking BCL §623(k), which provides that generally an appraisal proceeding constitutes a dissenting shareholder's exclusive remedy but makes an exception where the corporate action at issue was unlawful or fraudulent as to that shareholder, the amended complaint requested rescission or reformation of the merger and an accounting for the injuries inflicted on Briggs. The action was certified as a class action in August 1986 by Mark A. Costantino, *District Judge.* According to the district court docket entries, the action then lay inactive for some seven years.

In 1993, pursuant to Fed.R.Civ.P. 55, defaults were entered against Briggs and BAC, neither corporation being represented by counsel. In 1994, the court, Sterling Johnson, Jr., *District Judge*, entered a default judgment against those defendants on the issue of liability and ordered an inquest on damages. Also in 1994, the death of Edward Rosenstock was noted on the record. No executor or administrator was substituted for him, and the claims against him were abandoned.

In August 1997, pursuant to a stipulation among plaintiffs, Rosenstock, and Briggs (into which BAC

had been merged), the claims against Briggs and Rosenstock were resolved in a partial final judgment ("1997 Judgment"), David G. Trager, *District Judge*. The 1997 Judgment awarded the plaintiff class approximately $4 million against Briggs and approximately $6.9 million against Rosenstock. Pursuant to the stipulation, the 1997 Judgment also declared moot plaintiffs' state-court appraisal action.

In the meantime, in 1996, as discussed in Part II.C. below, plaintiffs had sought leave to file a second-amended and supplemental complaint, alleging new state-law claims against Rosenstock, Genser, and several new proposed defendants. That motion was denied.

B. *The October 1998 Dismissal of the Remaining Claims*

The above proceedings left pending only plaintiffs' claims against Genser. After entry of the 1997 Judgment, plaintiffs and Genser consented to have all further proceedings, including entry of judgment, conducted by a magistrate judge, and the matter was referred to Magistrate Judge Levy. Following a bench trial, the court, in a Memorandum and Order dated October 29, 1998 ("October 1998 Order"), and reported at 23 F.Supp.2d 326, dismissed the claims against Genser in their entirety.

With respect to the 1934 Act claims, the court noted that in order to succeed on a claim under §10(b) and Rule 10b-5, a plaintiff must prove a misrepresentation or omission as to a material fact in connection with the purchase or sale of a security, and an injury to the plaintiff caused by his reliance on the misrepresentation or omission. The district court assumed, *arguendo*, that plaintiffs could prove one or more material misrepresentations or omissions in the Briggs proxy statement regarding the merger that led to the forced sale of their Briggs shares. However, it concluded that, under the principle established by *Virginia Bankshares, Inc. v. Sandberg*, 501 U.S. 1083, 111 S.Ct. 2749, 115 L.Ed.2d 929 (1991), which involved claims that misrepresentations in proxy materials violated §14(a) of the 1934 Act, 15 U.S.C. §78n(a) (1994), plaintiffs had not established the causation element because their votes were not needed for approval of the Briggs-BAC merger.

The district court acknowledged that minority shareholders whose votes were unnecessary for approval of a freeze-out merger might nonetheless establish causation by showing that omissions or misrepresentations in the proxy statement had induced them to vote in favor of the merger and thereby caused them to forfeit an otherwise-available state-law remedy. *See* Virginia Bankshares, 501 U.S. at 1107, 111 S.Ct. 2749 (leaving open the possibility of that theory of

causation); *Wilson v. Great American Industries, Inc.*, 979 F.2d 924, 931 (2d Cir.1992) (upholding liability rulings in favor of shareholders on that theory of causation). In the present case, however, the district court concluded that causation on that theory had not been established because plaintiffs had the right to an appraisal of the fair value of their shares, and they did not show that they had forfeited that or any other state-law remedy as a result of the alleged fraud in the Briggs proxy statement. The court noted that, except in circumstances inapplicable here, New York law makes appraisal a dissenting shareholder's exclusive remedy:

> [t]he enforcement by a shareholder of his right to receive payment for his shares in the manner provided herein shall exclude the enforcement by such shareholder of any other right to which he might otherwise be entitled by virtue of share ownership.

N.Y. Bus. Corp. L. §623(k). Thus, the court rejected an argument by plaintiffs that but for the misleading nature of the proxy statement they could have obtained an injunction against the merger.

Given the exclusivity of plaintiffs' appraisal remedy, the district court also concluded that plaintiffs had no right to recover damages from Genser on their claims under state law. Although §623(k) goes on to state that "this section shall not

exclude the right of such shareholder to bring or maintain an *appropriate* action to obtain relief on the ground that such corporate action will be or is unlawful or fraudulent as to him," id. (emphasis added), the court concluded that the exception was inapplicable because plaintiffs' remaining claims against Genser sought only monetary relief:

> The "appropriate" action referred to in subdivision (k) has been held to be "one in which a dissenting shareholder seeks some form of equitable relief." *Breed [v. Barton*, 54 N.Y.2d 82, 87, 444 N.Y.S.2d 609, 429 N.E.2d 128, 130 (1981)]; *see also Burke v. Jacoby*, 981 F.2d 1372, 1380 (2d Cir.1992) ("An 'appropriate action' within the meaning of §623(k) is an action seeking equitable relief, and that type of action and the exercise of the right of appraisal are the dissatisfied stockholder's only avenues of relief."). As the New York Court of Appeals explained in *Breed*, limiting the exception in subdivision (k) to equitable relief "serves the valid function of denying dissenting shareholders the ability to reopen prior appraisal proceedings and again seek the identical relief merely by alleging fraudulent or unlawful corporate conduct in relation to the merger." *Breed*, [54 N.Y.2d at 87,] 444 N.Y.S.2d 609, 429 N.E.2d at 130. Although plaintiffs alleging fraud in an equitable proceeding under subdivision (k) may also seek money damages,

> the equitable relief must be the primary request, and such damages must be incidental to a grant of equitable relief. *Id.* [at 87, 444 N.Y.S.2d 609, 429 N.E.2d] at 131; see also Burke, 981 F.2d at 1380 ("Money damages are not available except as ancillary to a grant of traditionally equitable relief.") ...; *Direct Media/DMI, Inc. v. Rubin*, 171 Misc.2d 505, 654 N.Y.S.2d 986, 989 (1997) ("[A] shareholder may not seek an appraisal and also commence a separate action to recover money damages for improper corporate action....").

Grace v. Rosenstock, 23 F.Supp.2d at 335-36. The court noted that although plaintiffs originally had requested principally equitable relief against all defendants, their claims against Briggs had been settled and their only remaining requests against Genser were for money damages:

> Nothing in plaintiffs' pre-trial or post-trial submissions indicates a desire on plaintiffs' part for the court to award equitable relief, other than "rescissory damages," i.e., money damages, against Genser.... Plaintiffs' counsel made no mention of any other remedies at trial, and in fact conceded that plaintiffs' claim against Genser is for monetary damages. *See* Tr. at 687 ("What we are concerned here with is a claim of breach of fiduciary duty, ... which is an action

> not for fair price alone, it's an action for damages....").
> *Id.* at 336 n. 8.

Accordingly, all of plaintiffs' claims against Genser were dismissed. This appeal followed.

II. DISCUSSION

On appeal, plaintiffs challenge the October 1998 Order dismissing their claims against Genser, contending principally that because the proxy statement was issued in support of a freeze-out merger, resulting in a forced sale, they should not have been required to show causation in order to recover under §10(b) or Rule 10b-5; they also contend that if required to prove causation, they met their burden. In addition, plaintiffs challenge the district court's rejection of their 1996 motion for leave to file a new complaint adding new state-law claims and new parties to the action. For the reasons that follow, we find no basis for reversal.

A. *The Dismissal of the Federal Claims Against Genser*

In challenging the dismissal of their federal claims against Genser, plaintiffs contend principally that Virginia Bankshares does not apply to actions brought under §10(b) and Rule 10b-5, and that even if Virginia Bankshares applies, they established

causation because they forfeited a state- law remedy in reliance on misrepresentations in and omissions from the proxy statement. We find no merit in these contentions.

1. The Causation Requirement

Section 10(b) of the 1934 Act, which is generally regarded as a catch- all provision with respect to securities-related fraud, *see, e.g., Chiarella v. United States*, 445 U.S. 222, 226, 234-35, 100 S.Ct. 1108, 63 L.Ed.2d 348 (1980), prohibits the use, in connection with the purchase or sale of any security, of

> any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors,

15 U.S.C. §78j(b). Rule 10b-5, which impliedly provides a private right of action, *see, e.g., Blue Chip Stamps v. Manor Drug Stores*, 421 U.S. 723, 730, 95 S.Ct. 1917, 44 L.Ed.2d 539 (1975), makes it unlawful, in connection with the purchase or sale of any security, to

> make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the

> circumstances under which they were made, not misleading,

17 C.F.R. §240.10b-5(b). Because the private right of action under §10(b) and Rule 10b-5 is implied rather than express, its boundaries are left to judicial inference. *See*, e.g., *Blue Chip Stamps*, 421 U.S. at 749, 95 S.Ct. 1917 ("No language in either of those provisions speaks at all to the contours of a private cause of action for their violation.").

In framing the contours of private rights of action implied under the 1934 Act, the courts have sought to exclude, as a matter of law, claims based on hypothetical circumstances or speculation. Early in the development of such actions under §10(b) and Rule 10b-5, which addresses fraud "in connection with" the purchase or sale of a security, this Court ruled that no private action under those provisions is available to persons who were neither buyers nor sellers of the relevant securities. *See Birnbaum v. Newport Steel Corp.*, 193 F.2d 461, 462-64 (2d Cir.), *cert. denied*, 343 U.S. 956, 72 S.Ct. 1051, 96 L.Ed. 1356 (1952). That principle was adopted by the Supreme Court in *Blue Chip Stamps*, in which the plaintiffs were persons who had been offered--but had declined to purchase--shares in *Blue Chip Stamps* Co. pursuant to an antitrust-related consent decree entered into between the United States and the company. *See* 421 U.S. at 725-26, 95 S.Ct. 1917. The plaintiffs contended that the company

had "intentionally made the prospectus overly pessimistic" in order to dissuade the plaintiffs from accepting the offer, and thereby allow the rejected shares to be sold to the public at a higher price. *Id.* at 726-27, 95 S.Ct. 1917. The Supreme Court ruled that the district court had properly dismissed the suit. The Court reasoned that expanding the class of persons entitled to bring suit under Rule 10b-5 to include those who had neither bought nor sold shares would vastly increase the amount of frivolous securities litigation before the federal courts, in part because "the abolition of the *Birnbaum* rule would throw open to the trier of fact many rather hazy issues of historical fact the proof of which depended almost entirely on oral testimony." 421 U.S. at 743, 95 S.Ct. 1917.

Insofar as the element of causation is concerned, we have held in a variety of contexts that in order to establish a *prima facie* case under Rule 10b-5, a plaintiff must show, *inter alia*, both "*loss causation*--that the misrepresentations or omissions caused the economic harm," and "transaction causation--that the violations in question caused the [plaintiff] to engage in the transaction in question." Bennett v. United States Trust Co. of New York, 770 F.2d 308, 313 (2d Cir.1985) (internal quotation marks omitted) (emphases in original) (alleged misrepresentation as to margin rules), *cert. denied*, 474 U.S. 1058, 106 S.Ct. 800, 88 L.Ed.2d 776 (1986); *see also Burke v. Jacoby*, 981 F.2d 1372,

1378 (2d Cir.1992) (alleged misrepresentation in connection with corporate acquisition), *cert. denied*, 508 U.S. 909, 113 S.Ct. 2338, 124 L.Ed.2d 249 (1993); Citibank, N.A. v. K-H Corp., 968 F.2d 1489, 1494 (2d Cir.1992) (alleged misrepresentation in application for financing). We have also noted that both *loss causation* and transaction causation must be proven in the context of a private action under §14(a) of the 1934 Act and SEC Rule 14a-9 promulgated thereunder. *See Wilson v. Great American Industries, Inc.*, 979 F.2d 924, 931 (2d Cir.1992) (" Wilson "); Schlick v. Penn-Dixie Cement Corp., 507 F.2d 374, 381-82 (2d Cir.1974), *cert. denied*, 421 U.S. 976, 95 S.Ct. 1976, 44 L.Ed.2d 467 (1975), overruled on other grounds by Virginia Bankshares, 501 U.S. at 1100 n. 9, 1100-06.

As to the question presented here, i.e., whether transaction causation must be proven in connection with a securities-fraud claim based solely on misleading proxy statements and brought under §10(b) and Rule 10b-5, we find guidance in the decision of the Supreme Court in Virginia Bankshares with respect to claims of misleading proxy statements brought under §14(a) and Rule 14a-9, given that the interest in closing the floodgates to claims that are speculative or hypothetical is the same under both sets of provisions.

Section 14(a) makes it unlawful, by the use of the mails or any other instrumentality of interstate commerce, to solicit proxies "in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors...." 15 U.S.C. §78n(a). Rule 14a-9, promulgated thereunder, provides that

> [n]o solicitation subject to this regulation shall be made by means of any proxy statement ... containing any statement which, at the time and in the light of the circumstances under which it is made, is false or misleading with respect to any material fact, or which omits to state any material fact necessary in order to make the statements therein not false or misleading....

17 C.F.R. §240.14a-9(a) (1999). Section 14(a) and Rule 14a-9, like §10(b) and Rule 10b-5, do not expressly provide a private right of action. The Supreme Court recognized an implied private right of action for injury caused by a violation of §14(a), as implemented by Rule 14a-9, in J.I. Case Co. v. Borak, 377 U.S. 426, 84 S.Ct. 1555, 12 L.Ed.2d 423 (1964).

In Mills v. Electric Auto-Lite Co., 396 U.S. 375, 90 S.Ct. 616, 24 L.Ed.2d 593 (1970), the Court ruled that the causation requirement of Rule 14a- 9 would be satisfied where the challenged proxy statement

"was an essential link in the accomplishment of the transaction." *Id.* at 385, 90 S.Ct. 616. In that case, the majority shareholder held just over one-half of the corporation's outstanding shares, but the proposed merger could not be approved without the affirmative vote of two-thirds. Thus, the minority-shareholder plaintiffs were held to have satisfied the causation element because the merger could not have been authorized without the affirmative vote of at least some of the minority shares. The Mills Court left open the question of "whether causation could be shown where the management controls a sufficient number of shares to approve the transaction without any votes from the minority." *Id.* at 385 n. 7.

The Supreme Court answered that question in Virginia Bankshares, ruling that minority shareholders whose votes were not required for approval of the proposed freeze-out merger had failed to show that the materially misleading representations in the proxy statement violating Rule 14a-9 caused their injury. Although the plaintiff shareholders argued that the challenged proxy statement was an "essential link" within the meaning of Mills on the theory that their negative votes, though insufficient to defeat the merger, would have created sufficient bad publicity that the directors would not have proceeded with the merger, see 501 U.S. at 1100-01, 111 S.Ct. 2749,

the Virginia Bankshares Court found that theory too speculative:

> [I]n *Blue Chip Stamps* we raised concerns about the practical consequences of allowing recovery, under §10(b) of the Act and Rule 10b-5, on evidence of what a merely hypothetical buyer or seller might have done on a set of facts that never occurred, and foresaw that any such expanded liability would turn on "hazy" issues inviting self-serving testimony, strike suits, and protracted discovery, with little chance of reasonable resolution by pretrial process.... These were good reasons to deny recognition to such claims in the absence of any apparent contrary congressional intent.
>
> The same threats of speculative claims and procedural intractability are inherent in respondents' theory of causation linked through the directors' desire for a cosmetic vote. Causation would turn on inferences about what the corporate directors would have thought and done without the minority shareholder approval unneeded to authorize action. A subsequently dissatisfied minority shareholder would have virtual license to allege that managerial timidity would have doomed corporate action but for the ostensible approval induced by a misleading statement, and opposing claims of hypothetical diffidence and hypothetical boldness on the part

> of directors would probably provide enough depositions in the usual case to preclude any judicial resolution short of the credibility judgments that can only come after trial. Reliable evidence would seldom exist. Directors would understand the prudence of making a few statements about plans to proceed even without minority endorsement, and discovery would be a quest for recollections of oral conversations at odds with the official pronouncements, in hopes of finding support for ex post facto guesses about how much heat the directors would have stood in the absence of minority approval. The issues would be hazy, their litigation protracted, and their resolution unreliable. Given a choice, we would reject any theory of causation that raised such prospects, and we reject this one.

Virginia Bankshares, 501 U.S. at 1105-06, 111 S.Ct. 2749.

Although Virginia Bankshares addressed proxy-statement-fraud claims brought only under §14(a) and Rule 14a-9, its express reliance on the rationale of *Blue Chip Stamps*, a case involving §10(b) and Rule 10b-5, demonstrates that the same concerns compel the conclusion that the scope of the implied private right of action under either set of provisions does not encompass claims based on "a merely hypothetical ... set of facts that never occurred,"

Virginia Bankshares, 501 U.S. at 1105, 111 S.Ct. 2749. Plaintiffs have advanced no logical rationale--and we see none--for allowing a claimant to prevail on a misleading-proxy-statement claim under §10(b) and Rule 10b-5 without proving causation, when causation is required with respect to such a claim under §14(a) and Rule 14a-9, which deal expressly with misleading proxy statements, and is required under §10(b) and Rule 10b-5, which deal with claims of misleading statements in any medium. We conclude that the principle announced in Virginia Bankshares is applicable to misleading-proxy-statement claims that are brought under §10(b) and Rule 10b- 5, and that in order to prevail on such a claim, a plaintiff must present nonspeculative evidence of *loss causation* and transaction causation, see Wilson, 979 F.2d at 931.

We reject plaintiffs' contention that "[w]here the misrepresentations and nondisclosures under Rule 10b-5 are part and parcel of the forced sale by the plaintiffs shareholders ..., there is no separate requirement to show causation" (Plaintiffs' brief on appeal at 43). For that proposition, plaintiffs rely on Vine v. Beneficial Finance Co., 374 F.2d 627, 635 (2d Cir.), *cert. denied*, 389 U.S. 970, 88 S.Ct. 463, 19 L.Ed.2d 460 (1967). Quaere whether Vine would survive the rationale of Virginia Bankshares if Vine 's holding were as plaintiffs have characterized it; but in any event, in light of its actual holding, plaintiffs' *49 reliance is misplaced.

In Vine, we considered the complaint of a Class A shareholder who, after being subjected to a freeze-out merger, brought an action under §10(b) and Rule 10b-5 alleging that the defendant tender offeror had attained the share percentage needed to approve the freeze-out merger by fraudulently inducing Class A shareholders other than the plaintiff to tender their shares to it. We did not hold that the plaintiff was not required to plead reliance or causation; rather, we held that the complaint adequately pleaded both elements. Noting that the complaint alleged a single two-phase scheme to eliminate Class A shareholders, we stated that "[w]hat must be shown is that there was deception which misled Class A stockholders and that this was in fact the cause of plaintiff's claimed injury. The allegations of this complaint meet that test." *Id.* at 635.

In the present case, plaintiffs did not meet that test. Rosenstock and Genser at all pertinent times owned sufficient shares, either directly or through their ownership of BAC, to approve the Briggs-BAC merger, and there is no suggestion that they acquired those shares by means of fraud. No vote, sale of shares, or other action was required of minority shareholders in order to accomplish the merger.

In sum, Virginia Bankshares applies to claims of proxy fraud brought under §10(b) and Rule 10b-5,

and a plaintiff may not recover on such a claim without proving that his injury was caused by the fraud. Plaintiffs here, because minority-shareholder votes were not required for approval of the merger that was the subject of the proxy statements, did not show causation based on the approval of the merger.

2. Causation Based on Forfeiture of a State Remedy

The Virginia Bankshares Court left open the possibility that even minority shareholders whose votes were not necessary for approval of the proposed merger might nonetheless satisfy the causation requirement if they could show that the violations induced them to forfeit a state remedy. *See* 501 U.S. at 1107, 111 S.Ct. 2749. This Court addressed that issue in Wilson, in which the management had controlled sufficient shares to approve the proposed merger without the minority's votes, the plaintiff minority shareholders had been induced to vote in favor of the merger, and "their deceptively procured vote in favor of the merger deprived them of their state appraisal rights under" New York law, 979 F.2d at 930. We upheld the liability ruling in favor of the Wilson plaintiffs, stating as follows:

> We recognize that loss causation or economic harm to plaintiffs must be shown, as well as proof that the misrepresentations induced

> plaintiffs to engage in the subject transaction, that is, transaction causation. Here loss causation may be established when a proxy statement prompts a shareholder to accept an unfair exchange ratio for his shares rather than recoup a greater value through a state appraisal. And transaction causation may be shown when a proxy statement, because of material misrepresentations, causes a shareholder to forfeit his appraisal rights by voting in favor of the proposed corporate merger.

Wilson, 979 F.2d at 931.

> We noted that allowing that type of action does not pose a threat of "speculative claims and procedural intractability," ... because the forfeiture of state [remedies] is a question separate from the effectuation of the merger and does not require courts to guess how or whether the majority shareholders would have proceeded in the face of minority dissent.

Id. at 932 (quoting Virginia Bankshares, 501 U.S. at 1105.

In the present case, however, plaintiffs did not vote in favor of the merger and did not show that they relied on the proxy materials in any way that caused them to forfeit their rights to appraisal. Rather, plaintiffs contend, relying on Lynch v. Vickers

Energy Corp., 429 A.2d 497, 501 (Del.1981), overruled on other grounds, Weinberger v. UOP, Inc., 457 A.2d 701, 703-04 (Del.1983), that causation was established because they forfeited their state-law rights to obtain "rescissory damages" (Plaintiffs' brief on appeal at 51). We are unpersuaded for several reasons.

First, as the district court noted, see Part I.B. above, under New York law governing freeze-out mergers, except for an "appropriate" equitable action as envisioned by BCL §623(k), appraisal is the dissenting shareholders' exclusive remedy. Although the Lynch court held that a rescissory-damages remedy was available under Delaware law to the plaintiffs before it, the transaction at issue was not a freeze-out merger but a tender offer by the corporation's majority shareholder, and no appraisal remedy was available. We are not persuaded that Lynch, in which there was no forced sale and the tendering shareholders had no appraisal remedy, is authority for the proposition that rescissory damages were available under New York law in the present case where there was a forced sale, there was an appraisal remedy, and the pertinent statute provided that appraisal was the exclusive remedy. Plaintiffs cite no case applying New York law, and we know of none, that authorizes an award of rescissory damages for a freeze-out merger as to which a dissenting shareholder had a right of appraisal.

Second, though Lynch held that rescissory damages may be available as an equitable substitute for rescission where, because of mergers, the latter remedy is as a practical matter no longer feasible, plaintiffs have cited no authority suggesting that a monetary award in favor of a shareholder against a director would be viewed as anything other than an award of damages at law in circumstances where, as here, the plaintiffs have already settled their claims against the party that purchased their shares--i.e., the only entity against which rescission would be even a theoretically permissible remedy.

Third, we note that under Lynch, rescissory damages may reflect increases in the corporation's value subsequent to the challenged transaction and that plaintiffs in the present action apparently seek to benefit from a "surge in land values" through a date at least "30 months after the [Briggs] merger" (Plaintiffs brief on appeal at 51). Here, however, the pertinent defendants lawfully owned sufficient shares to approve the merger and freeze out other shareholders without the approval of any minority shares. Lynch did not involve such circumstances, and plaintiffs have not cited any New York case to support their suggestion that, in the circumstances here, an action for rescissory damages encompassing post-merger surges in land values would be considered an "appropriate" action within the meaning of §623(k).

Finally, we note that although plaintiffs no longer have appraisal rights, that is not the result of any reliance on the Briggs proxy statements. Rather, their appraisal suit was declared moot pursuant to their stipulation leading to the 1997 Judgment, which awarded the plaintiff class some $11 million from Briggs and Rosenstock. We see no forfeiture there.

In sum, plaintiffs have cited no New York law, or any other relevant authority, for the proposition that there was any available state-law remedy that they forfeited in reliance on the Briggs proxy statement. Accordingly, since their votes were not needed for approval of the merger, the district court correctly concluded that they failed to prove causation as required by §10(b) and Rule 10b-5.

B. *The Dismissal of the State-Law Claims*

Plaintiffs contend that the district court erred in finding their state-law claims against Genser barred by BCL §623(k) because it mistakenly believed that those claims sought primarily money damages rather than equitable relief. Plaintiffs argue that those claims must be viewed as requests for equitable relief because a February 1986 order of Judge Costantino effectively so characterized them. We disagree.

First, even if Judge Costantino's characterization of the claims constituted an order, it plainly was interlocutory. All interlocutory orders remain subject to modification or adjustment prior to the entry of a final judgment adjudicating the claims to which they pertain. *See* Fed.R.Civ.P. 54(b); Cullen v. Margiotta, 811 F.2d 698, 708 (2d Cir.), *cert. denied*, 483 U.S. 1021, 107 S.Ct. 3266, 97 L.Ed.2d 764 (1987), overruled on other grounds, Agency Holding Corp. v. Malley-Duff & Associates, 483 U.S. 143, 107 S.Ct. 2759, 97 L.Ed.2d 121 (1987); United States v. LoRusso, 695 F.2d 45, 53 (2d Cir.1982) ("whether the case sub judice be civil or criminal[,] so long as the district court has jurisdiction over the case, it possesses inherent power over interlocutory orders, and can reconsider them when it is consonant with justice to do so" (internal quotation marks omitted)), *cert. denied*, 460 U.S. 1070, 103 S.Ct. 1525, 75 L.Ed.2d 948 (1983).

Second, the posture of the case changed significantly in the 12 years between Judge Costantino's characterization of it in 1986 and the magistrate judge's analysis in 1998. Judge Costantino dealt only with the pleadings, and, aside from a typical catchall paragraph that mentioned damages, the only relief requested by the amended complaint was equitable. On the claims against Briggs, it requested rescission of the merger or reformation of its terms; on the derivative claim on

behalf of Briggs, it sought from the individual defendants an accounting and disgorgement of profits. By the time of trial in 1998, however, plaintiffs had settled their claims against Briggs, the purchaser of their shares; plaintiffs thus could no longer seek rescission. Nor were there any remaining derivative claims, as Briggs was no longer a party. Thus, as the district court observed in its October 1998 Order, plaintiffs' counsel stated at trial that " '[w]hat we are concerned here with is a claim of breach of fiduciary duty, ... which is an action not for fair price alone, it's an action for damages....' " 23 F.Supp.2d at 336 n. 8 (quoting Tr. 687). We note that, in the wake of that ruling, plaintiffs made no effort to suggest, by way of a motion for reconsideration by that court, that the court had misapprehended the nature of their remaining claims against Genser.

We see no error in the district court's characterization or dismissal of plaintiffs' state-law claims against Genser.

C. The Proposed Second Amended and Supplemental Complaint

In January 1996, more than a decade after commencing this action, plaintiffs sought leave to file a "Supplemental and Second Amended Complaint" ("Supplemental Complaint"), which would have added state-law claims against (a)

Rosenstock and Genser, (b) Bank Leumi Trust Company of New York ("Bank Leumi"), David Mack, Leo V. Berger, and Apex Marine Corp. (collectively the "proposed creditor defendants"), and (c) Gary Holman, an attorney for Briggs. Plaintiffs asserted, *inter alia*, that after consummation of the freeze-out merger, Rosenstock and Genser had engaged in a scheme to "subvert the jurisdiction of this federal Court ... [and] to make any judgment rendered by this Court in this action unenforceable and of no practical value" (Supplemental Complaint P 47) by causing Briggs to transfer assets to themselves and to the proposed creditor defendants.

The Supplemental Complaint alleged that Rosenstock and Genser, in furtherance of that scheme, looted Briggs between November 1986 and August 1989 by mortgaging its property to secure loans from the proposed creditor defendants and using the proceeds of the loans primarily for their own personal benefit rather than for the benefit of Briggs. Those acts were alleged to have violated common law and various provisions of New York's Debtor and Creditor Law ("DCL"), see N.Y. Debt. & Cred. L. (McKinney 1990), to wit, id. §273 (conveyance by a person who is insolvent); id. §273-a (conveyance by a person who is a defendant in a pending action or who has a judgment docketed against him); id. §274 (conveyance by a person in business); and id. §276 (conveyance made with

intent to defraud). The proposed pleading also alleged that in January 1990, Briggs and Rosenstock sold Briggs real estate for approximately 20% below its fair market value in order to make payments to the proposed creditor defendants.

The Supplemental Complaint further alleged that each of the proposed creditor defendants accepted notes and mortgages from Briggs, knowing that the proceeds of the loans were being diverted to Rosenstock and Genser for their personal use. Bank Leumi was alleged to have known that Briggs would not be able to meet its obligations, would be forced to borrow additional funds, and would be forced to sell its real estate under duress. The Supplemental Complaint alleged that Holman had committed professional malpractice and breached fiduciary and contractual duties to Briggs and to plaintiffs by representing Briggs while also serving as attorney to Rosenstock and Genser in their personal capacities, and by supervising the allegedly fraudulent conveyances while knowing that they were fraudulent as to Briggs and plaintiffs.

The Supplemental Complaint principally sought awards of damages to plaintiffs and Briggs, including punitive damages from Rosenstock and Genser. It also sought nullification of a 1992 state-court foreclosure judgment that Bank Leumi had obtained against Briggs.

The proposed new defendants opposed plaintiffs' motion to file the Supplemental Complaint, arguing principally that there was no basis for federal jurisdiction over the claims against them and that the claims were barred by the applicable statutes of limitations. Magistrate Judge Levy (to whom the matter had not yet been referred for all purposes) denied the motion, and plaintiffs' objections to that denial were rejected by Judge Trager. Without deciding the jurisdictional questions, the court denied the motion on the grounds of futility and delay, as explained in the magistrate judge's Memorandum and Order dated September 30, 1996 ("September 1996 Order"), reported at 169 F.R.D. 473 (1996).

In that decision, the court noted that the new claims that plaintiffs moved to add were subject to a six-year statute of limitations. Because plaintiffs' motion was made in 1996 and the new claims focused on conduct alleged to have occurred principally in 1986-1989, the court concluded that filing of the Supplemental Complaint would likely be futile because most of the new claims appeared to be time-barred. Plaintiffs argued that the statute of limitations was no bar because the filing of their new claims should be deemed to "relate [ ] back" to the time of filing of their amended complaint, Fed.R.Civ.P. 15(c). The court rejected that contention, observing that the proposed pleading was not based on the events challenged in the

amended complaint but rather "related to the notes and mortgages that Briggs executed years later"; hence the amended complaint could not have provided notice of the new claims. September 1996 Order, 169 F.R.D. at 481-82. The court likewise rejected plaintiffs' contention that relation back was appropriate on the theory that plaintiffs were challenging a "continuing course of conduct"; the court pointed out that the amended "complaint alleged, in essence, a specific act of wrongdoing, i.e., a freeze-out merger, which is a distinct transaction from the subsequent note and mortgage transactions plaintiffs now seek to add." *Id.* at 482 (internal quotation marks omitted).

Plaintiffs also argued that in 1990, less than six years prior to their January 1996 motion to file the Supplemental Complaint, Briggs made mortgage payments to the proposed creditor defendants, raising the cash for those payments by selling real estate below fair market value, and that the fraudulent-conveyance claims under DCL S§273, 274, and 276 based on those payments were not time-barred. The district court disagreed, reasoning that "[t]he January 1990 loan payments cannot, by themselves, constitute fraudulent conveyances, since they are not events that are independent or separate from the original note and mortgage transactions." September 1996 Order, 169 F.R.D. at 482. In addition, the court stated that even if that argument had merit, it would deny leave

to add those claims to the suit in order to avoid delaying resolution of this hoary action:

> Even if the January 1990 payments could themselves be considered fraudulent conveyances, ... this court would nonetheless deny plaintiffs' motion to amend and supplement the pleadings to include allegations regarding those payments. At this late date in the proceedings[,] granting plaintiffs' motion would cause substantial further delays and prejudice to the proposed new defendants, who would now be required to re-open all of the depositions that have taken place thus far in the litigation and to conduct full document discovery.

Id. at 482 n. 5.

The court also rejected several other timeliness arguments advanced by plaintiffs, including equitable tolling and equitable estoppel. Noting that "the doctrine of equitable tolling applies 'where the facts show that the defendant engaged in conduct, often itself fraudulent, that concealed from the plaintiff the existence of [the] cause of action,' " id. at 483 (quoting Long v. Frank, 22 F.3d 54, 58 (2d Cir.1994), *cert. denied*, 513 U.S. 1128, 115 S.Ct. 938, 130 L.Ed.2d 883 (1995)), the court pointed out that this case was then more than 11 years old and that plaintiffs did not dispute that they

had known of the alleged fraudulent conveyances at least as early as 1993. The court found that plaintiffs "offer[ed] no adequate explanation as to why they were unable to conduct full discovery ... prior to 1993." September 1996 Order, 169 F.R.D. at 484. In addition, noting that the doctrine of equitable estoppel is applied " 'in cases where the plaintiff knew of the existence of his cause of action but the defendant's conduct caused him to delay bringing his lawsuit,' " id. (quoting Dillman v. Combustion Engineering, Inc., 784 F.2d 57, 61 (2d Cir.1986)), the court found that doctrine inapplicable because plaintiffs "d[id] not contend that any of the defendants or proposed defendants engaged in conduct that caused plaintiffs to delay bringing suit once they were fully aware of their claims," September 1996 Order, 169 F.R.D. at 484.

On this appeal, plaintiffs raise various challenges to the district court's denial of leave to file the Supplemental Complaint. In reviewing their challenges, we are mindful that leave to amend is to be granted "freely ... when justice so requires," Fed.R.Civ.P. 15(a); see also Foman v. Davis, 371 U.S. 178, 182, 83 S.Ct. 227, 9 L.Ed.2d 222 (1962); John Hancock Mutual Life Insurance Co. v. Amerford International Corp., 22 F.3d 458, 462 (2d Cir.1994). However, in determining whether leave to amend should be granted, the district court has discretion to consider, *inter alia*, the apparent "futility of amendment," Foman v. Davis, 371 U.S.

at 182, 83 S.Ct. 227; see also Ruffolo v. Oppenheimer & Co., 987 F.2d 129, 131 (2d Cir.1993) (per curiam). Amendment would likely be futile if, for example, the claims the plaintiff sought to add would be barred by the applicable statute of limitations. *See*, e.g., McGill v. Goff, 17 F.3d 729, 734 (5th Cir.1994). The court also has discretion to deny leave to amend "where the motion is made after an inordinate delay, no satisfactory explanation is offered for the delay, and the amendment would prejudice" other parties, Cresswell v. Sullivan & Cromwell, 922 F.2d 60, 72 (2d Cir.1990); see also Tokio Marine & Fire Insurance Co. v. Employers Insurance of Wausau, 786 F.2d 101, 103 (2d Cir.1986), or where the belated motion would unduly delay the course of proceedings by, for example, introducing new issues for discovery, *see, e.g.*, Ansam Associates v. Cola Petroleum, Ltd., 760 F.2d 442, 446 (2d Cir.1985). The district court's denial of leave to amend is reviewed only for abuse of discretion. *See*, e.g., Peterson v. Insurance Co. of North America, 40 F.3d 26, 31 (2d Cir.1994); United States v. Continental Illinois National Bank and Trust Co. of Chicago, 889 F.2d 1248, 1254 (2d Cir.1989).

1. The Refusal To Allow Assertion of the DCL §273-a Claims

Plaintiffs contend that their claims under DCL §273-a were not barred by the statute of limitations because at the time of plaintiffs' motion to file the Supplemental Complaint, those claims had not yet even accrued. For the reasons that follow, we agree that those claims had not yet accrued, but we conclude that this is not a basis for reversal.

Section 273-a provides that

> [e]very conveyance made without fair consideration when the person making it is a defendant in an action for money damages or a judgment in such an action has been docketed against him, is fraudulent as to the plaintiff in that action without regard to the actual intent of the defendant if, after final judgment for the plaintiff, the defendant fails to satisfy the judgment.

N.Y. Debt. & Cred. L. §273-a (emphasis added). To prevail on a claim under §273-a, a plaintiff must establish "(1) that the conveyance was made without fair consideration; (2) that the conveyor is a defendant in an action for money damages or that a judgment in such action has been docketed against him, and (3) that [the] defendant has failed to satisfy the judgment." Taylor-Outten v. Taylor, 248 A.D.2d 934, 935, 670 N.Y.S.2d 295, 296 (4th Dept.1998) (internal quotation marks omitted). Because "[t]he existence of an unsatisfied judgment is an essential

element of [§273-a]," Carey v. Crescenzi, 923 F.2d 18, 21 (2d Cir.1991) (internal quotation marks omitted); see also Frybergh v. Weissman, 145 A.D.2d 531, 531, 536 N.Y.S.2d 465, 466 (2d Dept.1988), the limitations period, which is six years, see N.Y. C.P.L.R. §213(1) (McKinney 1990), begins to run, at the earliest, on the date of the judgment, see Carey v. Crescenzi, 923 F.2d at 21.

The unsatisfied judgment at issue here is the judgment entered against Briggs in August 1997. That judgment had not yet been entered when plaintiffs moved in 1996 to file the Supplemental Complaint. Accordingly, the limitations period had not yet begun to run, and we agree with plaintiffs that the district court erred in viewing their DCL §273-a claims as time-barred.

Two factors, however, persuade us that that error does not warrant reversal. First, plaintiffs did not make their present nonaccrual argument with respect to the §273-a claim before the magistrate judge. Nor did they make any timely presentation of that argument to the district judge, for it was not mentioned to Judge Trager in their objections to the magistrate judge's September 1996 Order. To the contrary, plaintiffs' statement of their objections to the magistrate judge's statute-of-limitations ruling asserted, without any exception for claims under §273-a, that "the statute of limitations on a claim for fraudulent transfers is measured from the date of the

transfer." (Letter from Sidney Bender to Judge Trager, dated October 23, 1996, at 1.) Plaintiffs made no mention of their §273-a nonaccrual contention until January 1997, when they unsuccessfully asked the district court to certify statute-of-limitations issues to this Court. Accordingly, plaintiffs waived their nonaccrual objection to the magistrate judge's ruling.

Second, we are disinclined to remand for the court to exercise pendent jurisdiction over this state-law claim because all of the federal claims have now been dismissed.

> The decision to exercise pendent jurisdiction is vested in the sound discretion of the district court. United Mine Workers of America v. Gibbs, 383 U.S. 715, 725-28, 86 S.Ct. 1130, 16 L.Ed.2d 218 (1966) .... The discretion is limited, however, by the consideration that "[n]eedless decisions of state law should be avoided...." *Id.* at 726

Fay v. South Colonie Central School District, 802 F.2d 21, 34 (2d Cir.1986) (reversing district court's exercise of pendent jurisdiction as abuse of discretion where dismissal of federal claim was required and state-law questions were unsettled). In United Mine Workers v. Gibbs, 383 U.S. 715, 86 S.Ct. 1130, 16 L.Ed.2d 218 (1966), the Supreme Court stated that "if it appears that the state issues

substantially predominate, whether in terms of proof, of the scope of the issues raised, or of the comprehensiveness of the remedy sought, the state claims may be dismissed without prejudice and left for resolution to state tribunals," id. at 726-27, 86 S.Ct. 1130; see also id. at 726, 86 S.Ct. 1130 ("Certainly, if the federal claims are dismissed before trial, even though not insubstantial in a jurisdictional sense, the state claims should be dismissed as well."); 28 U.S.C. §1367(c) (expressly authorizing district court, in actions commenced after December 1, 1990, see Judicial Improvements Act of 1990, Pub.L. No. 101-650, 104 Stat. 5089, 5114, to "decline to exercise supplemental jurisdiction" over a state-law claim over which it has no independent jurisdiction if "the district court has dismissed all claims over which it has original jurisdiction").

Given that plaintiffs did not timely raise their §273-a nonaccrual argument in the district court, that all federal issues have now been disposed of, and that the §273-a claims are substantially different from the federal claims that have been adjudicated, we conclude that it would be inappropriate to remand to the district court for the belated introduction and litigation of these state-law claims in federal court.

2. The Other Proposed Claims

Plaintiffs also challenge the district court's rejection of their theories as to why their proposed claims under other DCL sections were timely. We see no error in the district court's rulings with respect to those claims. Plainly, most of the claims were based on transactions that occurred more than six years prior to plaintiffs' motion to amend. Further, as to the 1990 payments made less than six years prior to the motion, the district court stated that even if those payments themselves could be considered fraudulent conveyances within the limitations period, the court would not allow plaintiffs to add those claims, given, *inter alia*, the belated timing of the motion and the fact that discovery would have to be reopened. We see no abuse of discretion in that ruling.

Moreover, even if we concluded that the district court's views of the timeliness of the proposed claims under DCL §§273, 274, and 276 were flawed, we would decline, for the reasons just discussed with respect to §273-a, to remand for the district court to adjudicate those state-law issues now that all federal issues have been resolved.

We note that plaintiffs, concerned with the possible preclusive effect of the district court's denial of leave to file the Supplemental Complaint, contend that the district court could not properly consider whether their new claims would be barred by the statute of limitations without first determining that

it had subject matter jurisdiction over those claims. For that proposition, plaintiffs rely on Arrowsmith v. United Press International, 320 F.2d 219 (2d Cir.1963) (en banc). Their reliance is misplaced, however, as their contention misperceives both the nature of the decision on a motion for leave to amend and the nature of pendent jurisdiction.

Arrowsmith did not involve a plaintiff's motion to amend the complaint; nor did it involve pendent jurisdiction. Rather, it concerned a defendant's motion to dismiss the complaint on the grounds of, *inter alia*, lack of personal jurisdiction and failure to state a claim on which relief can be granted. We held that the court should have resolved the jurisdictional issue, determining whether it had the power to adjudicate the action against that defendant, before dismissing for failure to state a claim, because a dismissal on the latter ground has preclusive effect. Neither of those grounds, however, was discretionary. If the action was flawed in either respect, the court was required to dismiss.

In contrast, as discussed above, both the decision whether to exercise pendent jurisdiction and the decision whether to allow a new pleading are committed to the sound discretion of the district court, *see, e.g.*, United Mine Workers v. Gibbs, 383 U.S. at 725-28, 86 S.Ct. 1130 (pendent jurisdiction); Foman v. Davis, 371 U.S. at 182, 83 S.Ct. 227

(amended pleading), and we have suggested that generally the denial of leave to bring in new defendants does not have preclusive effect with respect to the claims against those defendants, see Northern Assurance Co. of America v. Square D Co., 201 F.3d 84 (2d Cir.2000). In any event, both types of decision in question here are discretionary, and we see no requirement, in circumstances such as these, that either branch of discretion be exercised before the other.

CONCLUSION

We have considered all of plaintiffs' arguments on this appeal and have found in them no basis for reversal. The judgment of the district court is affirmed.

APPENDIX B

UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

At a stated term of the United States Court of Appeals for the Second Circuit, held at the United States Courthouse, Foley Square, in the City of New York, on the 26th day of October two thousand.

Grace

v. Dkt No: 98-9618

Genser

A petition for panel rehearing and a petition for rehearing en banc having been filed herein by the appellant Lorraine Grace et. al.

Upon consideration by the panel that decided the appeal, it is Ordered that said petition for rehearing is **DENIED**.

It is further noted that the petition for rehearing en banc has been transmitted to the judges for the court in regular active service and to any other judge that

heard the appeal and that no such judge has requested that a vote be taken thereon.

FOR THE COURT
ROSEANN B. MACKECHNIE, Clerk

By: /s/
Beth J. Meador
Administrative Attorney

Filed U.S. Court of Appeals for the Second Circuit, October 26, 2000

ROSEANN B. MACKECHNIE, CLERK

APPENDIX C

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

----------x

LORRAINE GRACE, et al.,

Plaintiff,

- against -

ROBERT ROSENSTOCK,
ROBERT GENSER, et. al.,

Defendant.

----------x

JUDGMENT
85-CV-2039 (DGT)

An order of the Honorable David G. Trager, United States *District Judge*, having been filed on August 5, 1997, no just reason for delay, entering judgment in favor of plaintiffs class against defendant Robert Rosenstock in the amount of $6,912,288.00; entering judgment in favor of plaintiffs class against defendant Briggs Leasing Corporation in the amount of $4,028,000.00; continuing this action by plaintiffs class against defendant Robert Genser which action is hereby severed and adjourned based on the representation that defendant Genser will file a petition in

bankruptcy on or before September 29, 1997; directing tha the action in Supreme Court of the State of New York, County of New York, Index No. 96/600193, is moot only as to defendant Robert Rosenstock; and, directing that the action by plaintiff as petitioners in the Supreme Court of the State of New York, County of Nassau (Index No. 13312, 1985), against Briggs Leasing Corporation, respondent, to fix the fair value of petitioners' shares as dissenting shareholders under Section 623 of the Business Corporation Law is moot, it is

ORDERED and ADJUDGED that final judgment is hereby entered in favor of the plaintiffs class against defendant Robert Rosenstock in the amount of $6,912,288.00; that final judgment is hereby entered in favor of plaintiffs class against defendant Briggs Leasing Corporation in the amount of $4,028,000.00; that this action shall continue by plaintiffs class against Robert Genser which action is hereby severed and adjourned based on the representation that defendant Genser will file a petition in bankruptcy on or before September 29, 1997; that the action in Supreme Court of the State of New York, County of New York, Index No. 96/600193, is moot only as to defendant Robert Rosenstock; and, that the action by plaintiffs as petitioners in the Supreme Court of the State of New York, County of Nassau (Index No. 13312, 1985), against Briggs Leasing Corporation, respondent, to fix the fair value of

petitioners"shares as dissenting shareholders under Section 623 of the Business Corporation Law is moot.

DATED: Brooklyn, New York
August 12, 1997

ROBERT C. HEINEMANN
Clerk of the Court

By: /s/
James Giokas
Chief Deputy Clerk

Filed Clerk's Office
U.S. District Court EDNY
August 15, 1997

APPENDIX D

United States District Court,
E.D. New York.

Oliver R. GRACE, Lorraine Grace, Morgan H. Grace and Gerald I. White, Trustee of the John E. Grace Trust, individually, and as stockholders of Briggs Leasing Corporation suing on behalf of themselves and for the benefit of said corporation and for the class of all other stockholders of said corporation similarly situated,

Plaintiffs,

— v.—

Robert ROSENSTOCK, Robert Genser, Edward Rosenstock, Briggs Leasing Corporation and Briggs Acquisition Corporation,

Defendants.

No. 85-CV-2039 (RML).

MEMORANDUM AND ORDER

LEVY, United States Magistrate Judge. Plaintiffs [FN1] are minority shareholders of defendant Briggs Leasing Corporation, [FN2] a public corporation that was in the business of leasing automobiles to individuals and businesses. They

commenced this action individually, as a class, and derivatively to rescind and reform a "freeze-out" merger, under federal and state law, and for money damages and other appropriate relief. Plaintiffs' amended complaint, filed on July 1, 1985, [FN3] alleges that the merger violated Section 10(b) of the Securities Exchange Act of 1934, Rule 10b-5 promulgated thereunder, N.Y.Bus.Corp.Law §605(a), and the exception stated in Section 623, subd. (K) of the N.Y. Bus. Corp.Law. [FN4] Plaintiffs also seek damages for breach of fiduciary obligation under New York state law.

FN1. Named plaintiffs Oliver R. Grace and Morgan H. Grace are deceased. By order dated November 6, 1996, plaintiffs were permitted to substitute named plaintiff Lorraine Grace, as Executrix of the Estate of Oliver R. Grace, for Oliver R. Grace and plaintiff Gerald I. White, as Executor of the Estate of Morgan H. Grace, for Morgan H. Grace in this action.

FN2. The named plaintiffs were the beneficial owners of 7,476 common shares of Briggs, or approximately 1.25 percent of the 595,728 outstanding shares of Briggs common stock. (*See* Plaintiffs' Pre-Trial Memorandum at 3.) As of September 25, 1985, Briggs had approximately 190 shareholders. (*Id.*) Robert Rosenstock's sister and brother-in-law, Adrienne Rosenstock Halperin and James Halperin, owned 79,170 shares of Briggs, or

approximately 13 percent of the outstanding common stock. (*Id.* at 5 n. 2.)

FN3. Plaintiffs originally commenced this action by a complaint dated June 3, 1985.

FN4. By order dated September 30, 1996, the court granted plaintiffs' motion to withdraw their claim under the Martin Act, N.Y.Gen.Bus.Law §352-c.

By order dated August 14, 1986, the Honorable Mark A. Costantino, United States *District Judge*, granted plaintiffs' motion to certify this action as a class action, pursuant to Rules 23(a) and 23(b) of the Federal Rules of Civil Procedure. By order dated March 17, 1994, the Honorable Sterling Johnson, Jr., United States *District Judge*, entered a default judgment on the issue of liability against defendants Briggs Leasing Corporation ("Briggs") and Briggs Acquisition Corporation. Judge Johnson further ordered that plaintiffs be permitted to conduct discovery as necessary and directed that an inquest on damages be held. On August 12, 1997, pursuant to a stipulation so ordered by the Honorable David G. Trager, United States *District Judge*, judgment was entered against Briggs in the amount of $4,028,000 and against Robert Rosenstock, the Vice President and a Director of Briggs, in the amount of $6,912,288. Defendant Edward Rosenstock, the former Chairman, Chief Executive Officer, and President of Briggs, is

deceased and no estate has been substituted for him. By stipulation dated November 7, 1997, the remaining parties consented to refer this case to a Magistrate Judge for all purposes, including the entry of judgment.

The primary transaction charged in the amended complaint is the alleged freeze-out merger, on or about February 26, 1985, of the minority shareholders of Briggs. Plaintiffs claim that the self-interested defendants effectuated the merger through the use of a materially false proxy statement, thereby freezing out the minority shareholders at the allegedly inadequate price of $1.50 per share. Specifically, the amended complaint charges that the proxy statement was materially misleading in that it failed to disclose, among other things, the improper diversion of corporate opportunities by Robert Rosenstock ("Rosenstock") and Robert Genser ("Genser"), who collectively owned seventy-two percent of the outstanding stock of Briggs. The bench trial against Robert Genser, the sole remaining defendant in this case, commenced on March 30, 1998 and ended on April 2, 1998.

BACKGROUND

Robert Genser was a Vice President, Secretary-Treasurer and Director of Briggs. (Trial Transcript ("Tr.") at 352; Plaintiffs' Exhibit 1 at 2.) On

January 10, 1985, Genser and Rosenstock each contributed all of their shares in Briggs (29,961 and 384,350 shares, respectively) to Briggs Acquisition Corporation ("BAC"), a shell corporation, and received one share of common stock of BAC in exchange for each share of Briggs. As a result of that transaction, Genser and Rosenstock became the sole shareholders of BAC. After an additional contribution of 17,516 shares of Briggs stock by Rosenstock (which he purchased from his father, Edward Rosenstock, for $1.50 per share), BAC owned approximately seventy-two percent of the outstanding common stock of Briggs.

By letter dated January 28, 1985, Briggs notified its shareholders that a special meeting would be held on February 25, 1985 for the purpose of voting on the proposed merger of BAC and Briggs, with Briggs to be the surviving company wholly owned by Genser and Rosenstock. The letter informed the shareholders, however, that "irrespective of the vote" of the minority shareholders, approval of the merger was assured because BAC, as the majority stockholder, planned to vote in favor of the merger. The notice also informed the shareholders that they would be bought out at $1.50 per share upon consummation of the merger.

The purported reason for the merger was to relieve Rosenstock and Genser of the burden of personally guaranteeing the debt of a public corporation.

Briggs had obtained a fair amount of credit from General Motors Acceptance Corporation ("GMAC") in connection with its purchases of automobiles and, in order to induce GMAC to extend such credit--which in January 1985 was in the amount of approximately $14 million--both Rosenstock and Genser had executed personal guarantees on the debt. As Briggs began to suffer reduced profits, allegedly as a result of increased competition in the auto leasing business from the major automobile manufacturers, Rosenstock and Genser decided to take the company private, purportedly in the hopes of turning it into a franchise for one of the major automobile manufacturers. (Trial

Memorandum of Robert Genser at 3-4.)
Attached to the notice of the special meeting was a proxy statement which explained, *inter alia*:

> [I]t is proper for Rosenstock and Genser to have the total ownership, and receive all of the earnings, of the Company [because they personally guaranteed the company's debt incurred by purchasing automobiles].... Rosenstock and Genser believe that they should receive the full benefit of any future increase in the equity and earnings of the Company. (Plaintiffs' Exhibit 1 at 6.) The proxy statement further explained that Briggs had hired Prudential-Bache Securities to render an opinion

on the appropriate price for shares owned by the minority shareholders, who would lose their interests in Briggs as a result of the merger. Based on its review of the corporate records, Prudential-Bache gave the Board of Directors an opinion that $1.50 per share would be a fair price for the minority stock. (*Id.* at 10.)

In addition, the proxy statement listed the book value of Briggs's real estate as $884,503, but disclosed an accumulated appreciation of $419,031 and noted that the company had recently obtained a first mortgage loan on the property in the face amount of $1 million. With regard to the real estate, the financial statement disclosed that there had been some preliminary discussions with architects and community officials about development of the property, but that no such plans had been finalized and that land use regulations "may restrict or totally eliminate the company's ability to continue to conduct its business at such premises." (*Id.* at 15.)

Finally, the proxy statement revealed that any shareholders dissenting from the merger had the right, pursuant to section 623 of New York's Business Corporation Law, to seek an appraisal by filing a written objection with the company prior to the vote. The proxy statement described the appraisal process in detail, and the full text of

section 623 was annexed to it. (*Id.* at 11-13; C-1-C-5.)

At the meeting on February 26, 1985, plaintiffs voted against the merger. Nonetheless, based solely on BAC's vote, the proposal was adopted and the merger became effective, with Genser and Rosenstock remaining as the sole shareholders of Briggs, Genser owning seven percent (7%) and Robert Rosenstock owning ninety-three percent (93%) of the common stock.

All of the above facts are undisputed. (*See* Joint Pretrial Order, dated June 27, 1997, at 1-3.) The parties' dispute centers around the valuation of the shares of Briggs and whether or not the proxy statement accompanying the notice of special meeting contained materially misleading misrepresentations and omissions concerning the value of the shares. According to plaintiffs, the fair value of Briggs, based on the true value of its real estate holdings at the time, was in excess of $5.00 per share. They claim, based on an appraisal of the real estate that was conducted in 1987, that Rosenstock and Genser deliberately "timed the merger to take advantage of the upward surge in the value of its real estate, and thus to deprive the plaintiffs from participating in that dramatic improvement value."

Plaintiffs also contend that the proxy statement accompanying the notice of special meeting contained materially misleading representations and omissions because it failed to disclose that the individually named defendants voted for and approved the merger because it was a necessary step in the consummation of a plan and scheme to divert to the individually named defendants, as sole shareholders of BRIGGS, the real property owned by BRIGGS which, once diverted to their sole control, was to be developed or sold for the 100% personal benefit of Rosenstock and Genser.

(Plaintiffs' Pre-Trial Memorandum at 7.) The proxy statement represented that it was proper for Genser and Rosenstock to own one hundred percent of Briggs and receive all of its income because they personally guaranteed the company's debts. Plaintiffs contend, however, that the proxy statement failed to disclose that Charlotte Rosenstock, Robert Rosenstock's mother, was the primary guarantor of those debts until January 1985. According to plaintiffs, Genser and Rosenstock first guaranteed the company's debts in late 1984, "when they did so for the first time in order to add an illusory business purpose and justification for the purported merger." *Id.* Plaintiffs further argue that, in fact, those guarantees, principally running to GMAC, "are in a real sense meaningless since such debt is fully collateralized by chattel mortgages on the purchased automobiles" and that it is therefore

"extremely unlikely that such guarantees would ever be called by General Motors." (*Id.* at 7-8.)

Plaintiffs also argue that the proxy statement was misleading in that it failed to disclose "the existence and value of legal claims of BRIGGS against the individually named defendants for repeated and long standing diversions of corporate funds for their own personal use and benefit." (*Id.* at 8.) Although the proxy statement listed each director's cash compensation for 1984, plaintiffs contend that "their actual and unreported compensation vastly exceeded those amounts" because those individuals had been using Briggs "as a personal cash box to defray tax-free the expenses incurred in pursuit of their opulent lifestyles" and charging Briggs excessive amounts and under- compensating it for its services in transactions between Briggs and companies owned by Rosenstock and Genser. (*Id.*)

Plaintiffs' primary contention, however, relates to Briggs's interest in real estate, which consisted of a fee interest in 67,000 square feet, and a lease on an additional 23,000 square feet under a long-term ninety-nine year lease, of property located at 777 Northern Boulevard in Great Neck, New York. (*Id.* at 7.) According to plaintiffs, the $1.50 share price offered to the minority shareholders was based on a valuation of Briggs's real estate at $479,000, when in fact it had a fair market value of $2,530,000. (Plaintiffs' Post-Trial Memorandum at 4.)

Plaintiffs also allege that Rosenstock and Genser caused Briggs to execute various notes and mortgages on that property, the proceeds of which went largely to Rosenstock and Genser personally (or were used for their personal benefit), to Belgrave Oldsmobile, Inc. and RER Motors, Inc. (companies owned by Rosenstock and Genser), or to Briggs Ford, an agency "that was going to be owned" by Robert Rosenstock and his mother, sister, and brother-in-law. (Plaintiffs' Pre-Trial Memorandum at 9-10.) As a result, plaintiffs claim that Rosenstock and Genser, as directors of Briggs, breached their fiduciary duties to Briggs and to plaintiffs by enriching themselves in the amount of "at least $6,314,000" at Briggs's expense and by causing Briggs to incur obligations that rendered it insolvent. (*Id.* at 11.)

Discussion

1. Causation Under Rule 10b-5

Rule 10b-5, promulgated under section 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. §78n, provides:

It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails or of any facility of any national securities exchange--

(a) To employ any device, scheme, or artifice to defraud,

(b) To make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or

(c) To engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person, in connection with the purchase or sale of any security.

17 C.F.R. §240.10b-5 (1996).

Section 10b-5 is a "catch all" that generally prohibits the use of manipulative or deceptive devices "in connection with" the purchase or sale of securities. David M. Brodsky & Daniel J. Kramer, Federal Securities Litigation 6-1 (1997). To sustain a claim under section 10b-5, a plaintiff must prove (1) a misrepresentation or omission; (2) of a material fact; (3) made with scienter; (4) that plaintiff relied upon; and (5) that caused plaintiff's injury. *See* Basic Inc. v. Levinson, 485 U.S. 224, 230-31, 108 S.Ct. 978, 99 L.Ed.2d 194 (1988); San Leandro Emergency Med. Group Profit Sharing Plan v. Philip Morris Cos., 75 F.3d 801, 808 (2d Cir.1996); Brown v. E.F. Hutton Group, Inc., 991 F.2d 1020, 1031 (2d Cir.1993).

At issue here is whether plaintiffs can demonstrate causation of damages, even assuming, *arguendo*, they can prove a misrepresentation made with the requisite scienter in connection with a purchase or sale of securities. *Virginia Bankshares, Inc. v. Sandberg*, 501 U.S. 1083, 111 S.Ct. 2749, 115 L.Ed.2d 929 (1991), controls. In that case, a shareholder who owned eighty-five percent of a company's stock moved to freeze out the remaining fifteen percent in a merger. The proxy statement concerning the vote on the proposed merger stated that the minority shareholders would be offered $42 per share, and that the directors believed this price was "fair" to the minority shareholders because $42 was a price above book value and market price. The evidence indicated, however, that the company possessed factual information suggesting that the minority shareholders' shares were worth at least $60 on the open market. *Id.* The Court held that such a dichotomy between the evidence in the company's possession and the particular dollar value it assigned to minority shareholders' shares in the proxy statement could be actionable as a material misrepresentation under S.E.C. Rule 14a-9, promulgated under the Securities Exchange Act of 1934 (the "34 Act"). *Id.* at 1097, 111 S.Ct. 2749.

The second issue in that case, however, was causation of damages. Justice Souter's majority opinion first discussed the Court's previous consideration of the causation issue in the context of

the implied private right of action arising under §14(a) of the '34 Act. It summarized Mills v. Electric Auto- Lite Co., 396 U.S. 375, 90 S.Ct. 616, 24 L.Ed.2d 593 (1970), in which the Court held that one could establish causation of damages by a materially misleading proxy solicitation by showing that the proxy solicitation was an "essential link" in the accomplishment of the transaction. Virginia Bankshares, 501 U.S. at 1100, 111 S.Ct. 2749 (citing Mills, 396 U.S. at 385, 90 S.Ct. 616). The Court then found that there was no causation in the case before it, and thus no implied private right of action, because the vote of the majority shareholder was legally sufficient to authorize the merger. *Id.* at 1106, 111 S.Ct. 2749. Because no other shareholder could affect the result of the voting, the proxy statement was not an "essential link" in accomplishing the freeze-out merger. *Id.* at 1102, 111 S.Ct. 2749.

The minority shareholders in Virginia Bankshares had posited two theories of causation. The first theory was that the directors' desire to avoid the minority shareholders' ill will by use of a misleading proxy solicitation provides the requisite causal nexus between the proxy statement and the merger. This theory was based on the premise that, in the face of an unfavorable minority shareholder vote, a board of directors might choose not to go forward with the transaction, even though the majority shareholder had the voting power to

singlehandedly authorize the transaction. The Court rejected this theory because it would "turn on inferences about what the corporate directors would have thought and done without the minority shareholder approval" and therefore would give rise to "speculative claims and procedural intractability." *Id.* at 1105-06, 111 S.Ct. 2749.

The second theory was that minority approval, while unneeded to authorize the transaction, would result in a loss of state law remedies. The plaintiffs argued that a favorable minority vote induced by a materially misleading proxy solicitation would preclude a minority suit attacking the merger on state law grounds, and that the forfeiture of such a state law remedy should be sufficient to demonstrate causation. The Court in Virginia Bankshares, although not rejecting this theory, declined to decide its merits because a favorable minority vote would not have rendered the transaction invulnerable to attack under Virginia law, which barred shareholders from seeking to avoid a transaction if the minority shareholders ratified the transaction following disclosure of the material facts and conflicts of interest. *Id.* at 1107-08, 111 S.Ct. 2749 (citing Va.Code Ann. §13.1-691(A)(2) (1989)). Because the plaintiffs could not demonstrate that the proxy solicitation actually resulted in the loss of state law remedy, the Court did not have to accept or reject the loss-of-state-law remedy theory of causation.

The Second Circuit, however, explicitly adopted the loss-of-state-law remedy causation theory in Wilson v. Great Am. Indus., Inc., 979 F.2d 924 (2d Cir.1992). In Wilson, minority shareholders sued the majority shareholders of the defendant corporation in a section 14(a) and Rule 14a-9 suit for injuries suffered because of a materially misleading proxy solicitation. The defendants had solicited the plaintiffs' votes for approval of a proposed freeze-out merger, although those votes were unnecessary to ratify the transaction. After exchanging their shares pursuant to the merger agreement and thereby forgoing their appraisal rights, the minority shareholders discovered that they had accepted an unfair exchange ratio for their shares based on material misrepresentations in the proxy statement. The plaintiffs based their suit on the theory of loss of a state law remedy--in this case appraisal rights. The Second Circuit held that minority shareholders may assert such a claim, though the court remanded the case for determination of whether the loss had actually occurred. *Id.* at 929-31; see also Howing Co. v. Nationwide Corp., 972 F.2d 700, 708-09 (6th Cir.1992) (holding that the loss of a state law remedy creates a federal action under §13(e) of the Securities Exchange Act), *cert. denied*, 507 U.S. 1004, 113 S.Ct. 1645, 123 L.Ed.2d 266 (1993); Thouret v. Hudner, No. 95 Civ. 1793(JSM), 1996 WL 38824, at *2-3 (S.D.N.Y. Feb. 1, 1996)

(holding that there was no private right of action under §14(a) where minority stockholder votes were "totally unnecessary and irrelevant to the passage of the directors' proposal for the election of directors at the annual shareholders' meeting," and distinguishing cases where "minority shareholders have given up state law remedies, such as appraisal rights, as a result of false and misleading statements contained in a proxy statement").

While Virginia Bankshares and Wilson addressed only claims under section 14(a), their reasoning and conclusions apply to all types of misrepresentations in connection with a merger, and therefore to claims brought under §10(b). *See* Scattergood v. Perelman, 945 F.2d 618, 625 (3d Cir.1991) (barring minority shareholders' §10(b) claims concerning freeze-out merger for lack of causation); Booth v. Connelly Containers, Inc., Civ. A. No. 89-8280, 1991 WL 171450, at *8 (E.D.Pa. Aug.30, 1991) (dismissing minority shareholders' 10b-5 claims and explaining that even if defendants had "misrepresented the value of [the] shares and capital assets, omitted material facts, and breached their fiduciary duties," the plaintiffs could not demonstrate causation under Virginia Bankshares because the defendants had the requisite votes to consummate the freeze-out merger); cf. Basic, Inc. v. Levinson, 485 U.S. at 231-32, 108 S.Ct. 978 (expressly adopting the standard of materiality set out in the §14(a) context as applicable to the §10(b)

context); Goldberg v. Meridor, 567 F.2d 209, 222 n. 3 (2d Cir.1977) ("The test for materiality under 14a-9 and 10b-5 is the same.").

Plaintiffs here do not contend that they waived any appraisal rights under New York law in reliance on the alleged misrepresentations in the proxy statement, or that an appraisal remedy was unavailable to them. Rather, applying the reasoning of Wilson to the instant case, plaintiffs argue that the allegedly deceptive proxy statement caused their injury "because the minority shareholders could have sought an injunction under New York law had the defendants not lulled the minority shareholders into security by the deceptive disclosure." (Letter from Sidney Bender to the Court, dated August 7, 1998, at 6 (emphasis added).) [FN5] However, plaintiffs cite no authority for the proposition that they would have been entitled to seek an injunction under New York State law. [FN6] Plaintiffs' claim for breach of fiduciary duty would not entitle them to injunctive relief--even if they were to prevail on that cause of action--but only to monetary damages. Benson v. RMJ Secs. Corp., 683 F.Supp. 359, 370 n. 17 (S.D.N.Y.1988). In addition, although injunctive relief is available under New York's Martin Act, N.Y.Gen.Bus.Law §352-c, (People v. Concord Fabrics, Inc., 83 Misc.2d 120, 371 N.Y.S.2d 550, 553 (Sup.Ct.N.Y. County 1975), aff'd, 50 A.D.2d 787, 377 N.Y.S.2d 84 (1st Dep't 1976)), that

remedy is only available to the State Attorney General, and not to private litigants (see Goldberg, 567 F.2d at 224 n. 7 (Meskill, J. dissenting); Loengard v. Santa Fe Indus. Inc., 639 F.Supp. 673, 676 (S.D.N.Y.1986), cause dismissed, 812 F.2d 712 (2d Cir.1987), certified question answered by, 70 N.Y.2d 262, 519 N.Y.S.2d 801, 514 N.E.2d 113 (1987); CPC Int'l Inc. v. McKesson Corp., 70 N.Y.2d 268, 275, 519 N.Y.S.2d 804, 514 N.E.2d 116 (1987)). However, as noted above, plaintiffs withdrew their Martin Act claim in this case on September 30, 1996.

FN5. I am compelled to note that plaintiffs raised this issue for the first time four months after the trial in response to a request from the court that they address the impact of Virgin Bankshares on their claims.

FN6. Although the amended complaint alludes to "[t]he likely ability to enjoin the merger under New York law" (Amended Complaint P 21), plaintiffs never specifically allege that they would have sought to enjoin the merger had the facts not been concealed.

Finally, although the Second Circuit in Goldberg held that the minority shareholders in that case had the ability to seek injunctive relief under New York State law, such relief was available because the shareholders had no appraisal right in that

transaction. *See* Goldberg, 567 F.2d at 219 ("Where an appraisal remedy is not available, the courts of New York have displayed no hesitancy in granting injunctive relief.") (emphasis added). The contrary is true here. Indeed, New York law is clear that where an appraisal proceeding is available, that remedy is exclusive, even if not exercised. Norte & Co. v. New York and Harlem R. Co., 222 A.D.2d 357, 635 N.Y.S.2d 629, 630 (1st Dep't 1995); see also Alpert v. 28 Williams St. Corp., 63 N.Y.2d 557, 568, 483 N.Y.S.2d 667, 473 N.E.2d 19 (1984) ("The pursuit of an appraisal proceeding generally constitutes the dissenting stockholder's exclusive remedy."); *Breed v. Barton*, 54 N.Y.2d 82, 85, 444 N.Y.S.2d 609, 429 N.E.2d 128 (1981) ("When [the dissenting shareholders] exercised the right ... to have their stock appraised in a judicial proceeding, they abandoned their alternative rights as shareholders."); Willcox v. Stern, 18 N.Y.2d 195, 201, 273 N.Y.S.2d 38, 219 N.E.2d 401 (1966) ("[W]here a merger is consummated in accordance with statutory procedures, the remedy of appraisal and payment is the only one available to dissenting stockholders."); Blumenthal v. Roosevelt Hotel, 202 Misc. 988, 115 N.Y.S.2d 52 (Sup.Ct.N.Y. County 1952) (denying injunction of corporate asset sale and dismissing complaint because statutory remedy of appraisal was exclusive). [FN7] Plaintiffs therefore would likely not have had the ability to seek injunctive relief.

FN7. As will be explained in more detail infra, an exception to the exclusivity of the appraisal remedy applies where a shareholder suing in his or her individual capacity seeks equitable relief based on the assertion that the corporate action is fraudulent or illegal. Pellman v. Cinerama, Inc., 503 F.Supp. 107, 110 (S.D.N.Y.1980) ("appraisal is not an exclusive remedy when the shareholder sues on grounds of fraud or illegality" and therefore "[f]ederal courts should invoke state appraisal proceedings as an exclusive remedy only when a complaint is clearly limited to state-law fiduciary claims"); Alpert, 63 N.Y.2d at 568, 483 N.Y.S.2d 667, 473 N.E.2d 19 ("An exception exists [to the exclusivity rule] when the merger is unlawful or fraudulent as to that shareholder, in which event an action for equitable relief is authorized."); see also N.Y.Bus.Corp.Law §623(k) (McKinney 1986) (enforcement of appraisal rights by a shareholder excludes enforcement of any other right to which he or she might otherwise be entitled, except "that this section shall not exclude the right of such shareholder to bring or maintain an appropriate action to obtain relief on the ground that such corporate action will be or is unlawful or fraudulent as to him"). However, plaintiffs' argument is that they "could" have sought an injunction "had the defendants not lulled the minority shareholders into security by the deceptive disclosure." Obviously, then, if there were no "deceptive disclosure," logic dictates that plaintiffs would not be able to assert

unlawful or fraudulent conduct and would therefore not have any right to equitable relief. Moreover, this court is aware of no New York case, and plaintiffs have certainly cited none, in which dissenting shareholders who had the right to procure an appraisal of their stock successfully sued to enjoin a corporate transaction.

At any rate, even if the remedy of seeking an injunction were available, to establish causation under this theory, plaintiffs must do more than simply assert that they would have sought to enjoin a transaction under state law if certain relevant information had been disclosed. They must show by a fair preponderance of the evidence that they would have succeeded in preventing the loss they sustained. Benson, 683 F.Supp. at 370 (citing Madison Consultants v. FDIC, 710 F.2d 57, 65 (2d Cir.1983)); see also Mayer v. Oil. Field Sys. Corp., 721 F.2d 59, 67 (2d Cir.1983) (plaintiff had to establish not only an available state court remedy, but that "he would have succeeded in preventing the loss he in fact suffered"). Plaintiffs have not even asserted a theory under which they might have been entitled to injunctive relief under state law, let alone attempted to meet their burden of demonstrating that such a claim would have been successful, and this court will not carry that burden for them. *See* Boone v. Carlsbad Bancorporation, Inc., 972 F.2d 1545, 1559 (10th Cir.1992) (dismissing Rule 14a-9 claims of minority

shareholders where plaintiffs "failed to affirmatively declare that certain withheld or misstated information would (or even probably would) have caused them to seek a state court injunction").

I therefore find that plaintiffs have failed to demonstrate a loss of a state law remedy sufficient to demonstrate causation under Rule 10b-5. Plaintiffs have not proved that they forfeited or otherwise lost any remedies under New York state law as a result of the alleged misrepresentations in the proxy statement. Accordingly, Virginia Bankshares mandates dismissal of plaintiffs' claims under §10(b) and Rule 10b-5.

2. Remedies Under New York State Law

Plaintiffs' remaining claims allege Briggs's failure, under New York law, to pay them "fair value" for their shares and seek monetary damages against defendant Genser for breach of fiduciary duty. 28 U.S.C. §1367(a) states: in any civil action of which the district courts have original jurisdiction, the district courts shall have supplemental jurisdiction over all other claims that are so related to claims in the action within such original jurisdiction that they form part of the same case or controversy under Article III of the United States Constitution.

Pursuant to 28 U.S.C. §1367(c)(3), a district court may decline to exercise supplemental jurisdiction over a state law claim under subsection (a) if "the district court has dismissed all claims over which it has original jurisdiction." Because plaintiffs' federal securities law claims have been dismissed, then, the court has discretion to dismiss plaintiffs' state claims for want of jurisdiction. Brotherhood of Locomotive Eng'rs Div. 269 v. Long Island R.R. Co., 85 F.3d 35, 39 (2d Cir.1996) (" 'When all bases for federal jurisdiction have been eliminated ..., the federal court should ordinarily dismiss the state claims.' ") (quoting Baylis v. Marriott Corp., 843 F.2d 658, 665 (2d Cir.1988)); see also Lennon v. Miller, 66 F.3d 416, 426 (2d Cir.1995) (dismissing supplemental state claim where court dismissed underlying federal claim); Block v. First Blood Assocs., 988 F.2d 344, 351 (2d Cir.1993) (refusal to exercise supplemental jurisdiction over investors' state law claims was proper upon dismissal of investors' federal securities claims); Shahzad v. H.J. Meyers & Co., 923 F.Supp. 57, 60-61 (S.D.N.Y.1996) (declining to exercise supplemental jurisdiction over state claims after dismissing investor's federal securities fraud claims); Bilick v. Eagle Elec. Mfg. Co., 807 F.Supp. 243, 257 (E.D.N.Y.1992) (because no federal claims remained, plaintiffs' state law claims relating to federal securities fraud action also had to be dismissed).

Nonetheless, if the court and the parties have expended substantial time and energy on the case prior to the disposition of the federal claim, the court may justifiably retain supplemental jurisdiction over state claims that derive from a common nucleus of operative fact. *See* Enercomp, Inc. v. McCorhill Pub., Inc., 873 F.2d 536, 545 (2d Cir.1989) (district court properly exercised pendent jurisdiction over state law claims where sole federal claim was dismissed during trial); Philan Ins. Ltd. v. Frank B. Hall & Co., 786 F.Supp. 345, 347 (S.D.N.Y.1992) (district court may exercise supplemental jurisdiction over state claims subsequent to dismissal of federal claims, despite lack of independent basis for jurisdiction, if substantial resources have already been expended in action). This case was filed over thirteen years ago, the trial has taken place, and both the parties and the court have devoted substantial resources in this action. Indeed, the original judge and at least three parties to this case have passed away since its inception, and further delays would be unwarranted. Accordingly, although the court is hard-pressed to understand why defendant Genser opted to defend this case at trial rather than attempt to resolve it by dispositive motion, in the interests of judicial economy the court will extend supplemental jurisdiction and address plaintiffs' state law claims.

As explained above, plaintiffs' state law claims derive from the New York Business Corporation

Law ("B.C.L.") and the common law concerning breach of fiduciary duty. Article 9 of the B.C.L. authorizes any two or more domestic corporations to merge into a single corporation, which shall survive as one of the constituent corporations participating in the merger. *See* B.C.L. §901. The B.C.L. establishes procedures for the approval of a plan of merger by the board of each constituent corporation (B.C.L. §902) and for its submission to the shareholders of each for their authorization by a two-thirds vote. *Id.* §903. Section 623 of the B.C.L. recognizes a shareholder's right to object to corporate action, including merger, and establishes procedures for a dissenting shareholder to elect and demand payment of the fair value of his or her shares. If the corporation fails to make a written offer to each electing shareholder to pay for his or her shares at a specified price that the corporation considers fair, or if any dissenting shareholder or shareholders disagree with the price offered, a special proceeding may be instituted in state court to determine the rights of the dissenting shareholders and to fix the fair value of their shares. *Id.* §623(g), (h). Either the corporation (id. §623(h)(1)) or the dissenter may institute such a proceeding (id. §623(h)(2)), but the latter may only act upon the former's failure to do so.

In the event an appraisal proceeding is commenced, B.C.L. §623(h)(4) provides:

> The court shall determine whether each dissenting shareholder ... is entitled to receive payment for his shares. If the ... court finds that any dissenting shareholder is so entitled, it shall proceed to fix the value of the shares, which, for the purposes of this section, shall be the fair value as of the close of business on the day prior to the shareholders' authorization date.

In addition, B.C.L. §623(k) provides, in pertinent part:

> The enforcement by a shareholder of his right to receive payment for his shares in the manner provided herein shall exclude the enforcement by such shareholder of any other right to which he might otherwise be entitled by virtue of share ownership, ... except that this section shall not exclude the right of such shareholder to bring or maintain an appropriate action to obtain relief on the ground that such corporate action will be or is unlawful or fraudulent as to him. (emphasis added)

It is the exception stated in subdivision (k) that plaintiffs invoke in support of their right to bring state law claims against Robert Genser in this action, which leads to the obvious question: what is an "appropriate" action?

The "appropriate" action referred to in subdivision (k) has been held to be "one in which a dissenting shareholder seeks some form of equitable relief."

Breed, 54 N.Y.2d at 87, 444 N.Y.S.2d 609, 429 N.E.2d 128; *see also Burke v. Jacoby*, 981 F.2d 1372, 1380 (2d Cir.1992) ("An 'appropriate action' within the meaning of § 623(k) is an action seeking equitable relief, and that type of action and the exercise of the right of appraisal are the dissatisfied stockholder's only avenues of relief."). As the New York Court of Appeals explained in *Breed*, limiting the exception in subdivision (k) to equitable relief "serves the valid function of denying dissenting shareholders the ability to reopen prior appraisal proceedings and again seek the identical relief merely by alleging fraudulent or unlawful corporate conduct in relation to the merger." *Breed*, 444 N.Y.S.2d 609, 429 N.E.2d at 130. Although plaintiffs alleging fraud in an equitable proceeding under subdivision (k) may also seek money damages, the equitable relief must be the primary request, and such damages must be incidental to a grant of equitable relief. *Id.* at 131; see also Burke, 981 F.2d at 1380 ("Money damages are not available except as ancillary to a grant of traditionally equitable relief.") (citation and internal quotations omitted); Staskus v. Rawlplug Co., No. 92 Civ. 3069, 1993 WL 212736, at *6 (S.D.N.Y. June 11, 1993) (shareholders' state law claims were barred by section 623(k) where plaintiffs expressed

no preference for rescission over appraisal and "appear [ed] to attach equal importance to each of their remedial choices"); *Direct Media/DMI, Inc. v. Rubin*, 171 Misc.2d 505, 654 N.Y.S.2d 986, 989 (Sup.Ct.N.Y. County 1997) ("[A] shareholder may not seek an appraisal and also commence a separate action to recover money damages for improper corporate action...."). [FN8]

FN8. Plaintiffs point out that in February of 1986, Judge Costantino denied a motion by Briggs and BAC to stay the proceedings in this court in order to permit appraisal proceedings to go forward in state court. In his Memorandum and Order, Judge Costantino held that the exception in §623(k) applied to this case because it was an equitable action. At that time, obviously, Briggs and BAC were parties to this action and plaintiffs were seeking the equitable remedy of rescission. Plaintiffs have since settled their claims against Briggs, Robert Genser is the sole remaining defendant in this case, and there is no indication that plaintiffs continue to seek any equitable relief. Nothing in plaintiffs' pre-trial or post- trial submissions indicates a desire on plaintiffs' part for the court to award equitable relief, other than "rescissory damages," i.e., money damages, against Genser. *See* Randall v. Loftsgaarden, 478 U.S. 647, 656, 106 S.Ct. 3143, 92 L.Ed.2d 525 (1986) (stating that under the rescissory measure of damages, "the plaintiff is entitled to a return of the

consideration paid, reduced by the amount realized when he sold the security and by 'any income' received on the security") (citation omitted). Plaintiffs' counsel made no mention of any other remedies at trial, and in fact conceded that plaintiffs' claim against Genser is for monetary damages. *See* Tr. at 687 ("What we are concerned here with is a claim of breach of fiduciary duty, ... which is an action not for fair price alone, it's an action for damages...."). Indeed, it is questionable whether this court would have the power to grant any form of equitable relief at this point in the case, when the corporation at issue is no longer a party. Plaintiffs have certainly provided no support for the proposition that it would.

At this point in the case, plaintiffs are no longer seeking any form of traditional equitable relief, such as dissolution or recission of the merger. Their state law claims against Robert Genser, as the sole remaining defendant in this case, seek purely monetary relief. Although plaintiffs' complaint originally requested the equitable remedy of rescission, the case--in its present state--seeks only damages. It therefore suffers from a "fatal absence of any primary request for equitable relief" (*Breed*, 54 N.Y.2d at 87, 444 N.Y.S.2d 609, 429 N.E.2d 128) and is barred by the rule of exclusivity set forth in section 623(k). *See* Walter J. Schloss Assocs. v. Arkwin Indus., Inc., 61 N.Y.2d 700, 472 N.Y.S.2d 605, 460 N.E.2d 1090 (1984) (adopting

dissenting opinion of Mangano, J.), rev'g, 90 A.D.2d 149, 455 N.Y.S.2d 844 (2d Dep't 1982); see also Burke, 981 F.2d at 1381 (affirming district court's dismissal of minority shareholder's state law claim for breach of fiduciary duty where complaint sought only compensatory and punitive damages and an accounting, but "made no attempt to obtain traditionally equitable relief such as a rescission").

In addition, derivative claims brought by shareholders on behalf of the corporation, and not in their individual capacities, do not fall under the exception to the exclusivity rule in §623(k). Norte & Co., 635 N.Y.S.2d at 630-31; see also *Breed*, 54 N.Y.2d at 86, 444 N.Y.S.2d 609, 429 N.E.2d 128 ("It is evident from the express language of subdivision (k) that this exception to the general rule of exclusivity of the appraisal remedy permits a shareholder to pursue an appropriate action only in his individual capacity and not as the instigator of a derivative suit."). Here, plaintiffs' claim against Genser for breach of fiduciary duty is derivative in nature. Norte & Co., 635 N.Y.S.2d at 630-31; see also Abrams v. Donati, 66 N.Y.2d 951, 953, 498 N.Y.S.2d 782, 489 N.E.2d 751 (1985) ("[A]llegations of mismanagement or diversion of assets by officers or directors to their own enrichment, without more, plead a wrong to the corporation only, for which a shareholder may sue derivatively but not individually."). It must therefore be dismissed for that reason, as well.

CONCLUSION

For the reasons stated above, this case is dismissed with prejudice.

SO ORDERED.
E.D.N.Y.,1998.
Grace v. Rosenstock

APPENDIX E

UNITED STATES DISTRICT COURT
EASTERN DISTRICT OF NEW YORK

----------x

OLIVER R. GRACE,
et al.,

Plaintiffs,

- against -

ROBERT ROSENSTOCK, et al.

Defendants

----------x

MEMORANDUM OF
DECISION AND ORDER
CV-85-2039(MAC)

February 1986

CONSTANTINO, D.J.

Defendants Briggs Leasing Corporation and Briggs Acquisition Corporation move this court to stay proceedings in this court to permit the appraisal proceedings in the Supreme Court, Nassau County entitled *Halperin et al. v. Briggs Leasing Corp./Index #9973* to go forward. We note that the

New York State Supreme Court on October 7, 1985 already stayed the State action pending resolution of this court's determination. Although we recognize a federal court's discretion to stay proceedings pending the disposition of a State court action we decline to do so in this action. As the Court of Appeals in *Alpert v. 28 William Street Corp.*, 63 N.Y. 2d 557, 568, 483 N.Y.S. 2d 667 stated: "The pursuit of an appraisal proceeding generally constitutes the dissenting shareholder's exclusive remedy (*see* Business Corporation Law, §623 subd[k]; *see also Breed v. Barton*, 54 N.Y. 2d 82, 85). An exception exists however, when the merger is unlawful of fraudulent as to that shareholder, in which event an action for equitable relief is authorized." (Business Corporation Law §623 subd[k]. *Alpert v. 28 William Street Corp.*, *supra* at 568. The exception 623k applies to the instant action as alleged in the plaintiff's complaint. Since the State Supreme Court granted the stay of the appraisal action under the authrity of *Alpert v. 28 William Street Corp.*, *supra*, the equitable action in this court will proceed. *See also Pellman v. Cinerama*, 503 F. Supp. 107 (S.D.N.Y. 1980).

Defendants Briggs Leasing Corporation and Briggs Acquisition move pursuant to Fed. R. Civ. P. 12(c) for an order granting judgment on the pleadings. Defendants' motion is denied in the entirety. Plaintiffs sufficiently plead a cause of action for fraud. The complaint adequately pleads a section

10(b) claim. Plaintiffs' ability to prove their claim at trial is a question of fact which is not appropriate for resolution at this stage of the litigation. Plaintiffs have adequately plead fraud in connection with the merger under 10(b) and have standing to maintain the instant action.

SO ORDERED.

/s/

U. S. D. J.

APPENDIX F

UNITED STATES DISTRICT COURT
EASTERN DISTRICT OF NEW YORK

----------x

OLIVER R. GRACE, LORRAINE GRACE, MORGAN H. GRACE and GERALD I. WHITE, Trustee of the JOHN E. GRACE TRUST, individually, and as stockholders of BRIGGS LEASING CORPORATION, suing on behalf of themselves and for the benefit of said corporation and for the class of all other stockholders of said corporation similarly situated,

Plaintiffs,

-against-

ROBERT ROSENSTOCK, ROBERT GENSER, EDWARD ROSENSTOCK, BRIGGS LEASING CORPORATION and BRIGGS ACQUISITION CORPORATION

Defendants.

----------x

AMENDED COMPLAINT -- CLASS ACTION

85 Civil 2039 (MAC)

Plaintiffs, by their attorneys, LEVENTRITT LEWITTES & BENDER, as and for their Complaint herein allege as follows:

1. This is a civil action - derivative, class, and individual - for equitable and other relief. It is based on violations of Section 10(b) of the Securities Exchange Act of 1934, as amended, 15 U.S.C. §78(j), Rule 10b-5 promulgated thereunder, N.Y. Bus. Corp. Law §605(a) and the exception stated in §623 subd. (k) of N.Y. Bus. Corp. Law, N.Y. General Bus. Law §352-c (the "Martin Act") and for breach of fiduciary obligation under New York State law. As to all defendants, this Court has federal question jurisdiction under §27 of the Securities Exchange Act of 1934 and pendent jurisdiction over the State claims.

CLASS ACTION ALLEGATIONS

2. Plaintiffs were shareholders of BRIGGS LEASING CORPORATION, a New York corporation ("BRIGGS") at the time of the transactions herein complained of. The class of shareholders plaintiffs seek to represent were also shareholders of BRIGGS at the time of the transactions herein complained of. There are approximately 190 members of the class, thus the class is so numerous that joinder of all is impracticable.

3. The principal transaction herein complained of involves the freeze-out merger on or about February 26, 1985, of the minority shareholders of BRIGGS by the self-interested majority defendant shareholders, without business purpose and at a totally unfair price (hereinafter referred to as "The Merger"). That purported merger was invalid, is subject to rescission and plaintiffs continue as constructive owners of an equity interest in BRIGGS.

4. The class members are identically situated – their claims involve the same transactions. Thus there are questions of law and fact common to the class. Plaintiffs' claims are typical of the claim of the class and plaintiffs will fairly and adequately protect the interest of the class – they have similar interests with those of the class and their counsel is experienced and able to conduct class action litigation. This action falls within the Federal Rules of Civil Procedure, Rule 23(b) (1) (A), b(1) (B) and 23 (b) (2) and b(3).

5. Common questions of law and fact predominate over questions affecting only individual members and a class action is superior to other available methods for the fair and efficient adjudication of the controversy; this case is ideal for class action status. Rule 23(b) (3) has been used quite frequently in cases, such as this, involving securities frauds. This action alleges misrepresentations and omissions from the proxy

statement dated January 28, 1985. On information and belief all the members of the class received that proxy statement. This action involves the same principal transaction – the freeze-out merger of all BRIGGS minority shareholders at an inadequate price.

COUNT I

6. As of February 25, 1985, BRIGGS had 595,728 shares of common stock outstanding. Plaintiffs were the beneficial owners of 7,476 common shares of BRIGGS, or approximately 1.25% of BRIGGS outstanding stock.

7. BRIGGS is a New York corporation which at all relevant times was engaged in the business of leasing automobiles, primarily Cadillac and Oldsmobile automobiles, to individuals and businesses. At all relevant times, BRIGGS was a public corporation, the shares of which have been traded over-the-counter. On information and belief, as of February 25, 1985, BRIGGS had approximately 190 shareholders. At the time of the purported merger, the reported book value of its common stock was approximately $2.75 a share.

8. Prior to January 10, 1985, the majority shareholders of BRIGGS were defendants ROBERT ROSENSTOCK ("ROSENSTOCK"), his father, EDWARD ROSENSTOCK and ROBERT GENSER ("GENSER"), who, in total, owned 72%

of BRIGGS. ROSENSTOCK was a Vice President and Director of BRIGGS. GENSER was Vice President, Secretary-Treasurer and Director of BRIGGS. EDWARD ROSENSTOCK was Chairman of the Board, Chief Executive Officer and President of BRIGGS.

9. ROSENSTOCK and GENSER, majority shareholders, directors and officers of BRIGGS, recently formed BRIGGS ACQUISITION CORPORATION ("BAC"), a New York corporation, for the sole purpose of facilitating the freeze-out merger between BRIGGS and BAC.

10. On January 10, 1985, ROSENSTOCK and GENSER contributed all of their respective shares of BRIGGS (384,350 and 29,961 shares, respectively) then owned by them to BAC, and received one share of common stock of BAC in exchange for each share of BRIGGS contributed by them. The sole shareholders of BAC are ROSENSTOCK and GENSER.

11. On January 14, 1985, ROSENSTOCK purchased 17,516 shares of BRIGGS from defendant EDWARD ROSENSTOCK, his father, for $1.50 per share. On the same date, ROSENSTOCK contributed all 17,516 shares of BRIGGS to BAC in exchange for 17,516 shares of BAC. Thus, BAC owned approximately 72% of the issued and outstanding

shares of the common stock of BRIGGS immediately prior to the merger.

12. By Notice dated January 28, 1985, BRIGGS mailed a letter to its shareholders notifying them that a special meeting would be held on February 25, 1985, for the purpose of voting upon the merger of BAC into BRIGGS, with BRIGGS the surviving company to be wholly-owned by ROSENSTOCK and GENSER. The Notice informed the shareholders, that "irrespective of the vote" of the minority shareholders, approval of the merger was assured because the (self-interested) majority stockholder BAC, solely owned by ROSENSTOCK and GENSER, was in favor of the merger and had agreed to vote same.

13. The Notice of Special Meeting informed the shareholders that they would be bought out at $1.50 per share upon consummation of the merger. That price is totally unfair and fraudulent.

14. Attached to the Notice of Special Meeting was a Proxy Statement which contained numerous material misrepresentations and omissions, specified herein below.

15. At the shareholders' meeting on February 25, 1985, plaintiffs voted against the merger. Based solely on BAC's vote of their shares

in BRIGGS, the merger proposal was purportedly adopted.

16. On February 26, 1985, the merger purportedly became effective, with ROSENSTOCK and GENSER remaining as the sole shareholders of BRIGGS. ROSENSTOCK now purportedly owns 93% of the common stock of BRIGGS and GENSER now purportedly owns the remaining 7%.

17. BAC is a shell corporation formed by the individually named defendants for the sole purpose of providing a vehicle by which the individually named defendants would freeze out the minority shareholders of BRIGGS. The merger had no business purpose, but rather was effected for the sole purpose of increasing the personal wealth of ROSENSTOCK and GENSER. The Proxy Statement (p. 6), stated:

> "it is proper for ROSENSTOCK and GENSER to have the total ownership and receive all of the earnings of the Company... ROSENSTOCK and GENSER believe they should receive the full benefit of any future increase in the equity and earnings of the Company."

18. The Proxy Statement employed by BRIGGS, BAC and the individually named defendants, in order to effectuate the merger, knowingly and intentionally constituted a device,

scheme and artifice to defraud BRIGGS minority shareholders. For the purpose of forcing the BRIGGS minority shareholders to surrender, and thereby sell, their stock pursuant to the merger plan, and thereby forgo the real value of said securities and a continuing interest in BRIGGS, the Proxy Statement contained numerous untrue statements of material facts and omitted to state material facts necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, all in violation of Section 10(b) of the Act and Rule 10b-5 promulgated thereunder: To wit:

a. The Proxy Statement failed to disclose that the individually named defendants voted for and approved the merger because it was a necessary step in the consummation of a plan and scheme to divert to the individually named defendants, as sole shareholders of BRIGGS, the real property owned by BRIGGS which, once diverted to their sole control, was and is to be quickly developed into an office building-supermarket complex for the personal benefit of the defendants. BRIGGS owns 67,000 square feet, and leases an additional 23,000 square feet under a long term lease, of prime realty located at 777 Northern Boulevard, Great Neck, New York, the value of which substantially exceeded the book value set forth in the financial statements appended to the Proxy Statement. Contrary to the representation in the Proxy Statement, these

development plans were well advanced and will be promptly implemented absent the relief sought herein.

b. The Proxy Statement represents the value of the real estate owned by BRIGGS as being $883,503. In fact, and undisclosed, that realty is worth at today's market value in excess of $2 million.

c. The Proxy Statement represented that the BRIGGS Board of Directors, *i.e.*, the individually named defendants, voted for and approved the merger because they concluded that it was proper for defendants GENSER and ROBERT ROSENSTOCK to own 100% of BRIGGS and receive all its income since they personally guaranteed the company's debt incurred by purchasing automobiles. On information and belief, and undisclosed, the primary guarantor of such debts until January, 1985, was CHARLOTTE ROSENSTOCK. GENSER and ROBERT ROSENSTOCK never guaranteed such debts until recently when they did so for the first time in order to add an illusory business purpose and justification for the purported merger. In fact, and undisclosed, such guarantees, principally running to General Motors Acceptance Corporation ("General Motors"), are in a real sense meaningless since such debt is fully collateralized by chattel mortgages on the purchased automobiles. It is extremely unlikely that such guarantees would ever be called by General Motors.

Rather than a security protection for General Motors, General Motors insists on such guarantees to insure continuity of ownership of entities in its distribution system. In any event, even if the guaranties were called, defendants GENSER and ROBERT ROSENSTOCK come nowhere near having the financial wherewithal to meet them, a fact well known to General Motors and the defendants.

d. On information and belief, the Proxy Statement fails to reveal offers from third parties to purchase BRIGGS real estate for sums substantially in excess of its reported value of $883,503. In particular, one such offer was for $1.5 million in addition to a continuing one-half interest in the property as redeveloped by the proposed buyer.

e. The Proxy Statement fails to disclose any description of the defendants' existing plans to develop the BRIGGS real estate, including estimates of the income to be generated by such development.

f. On information and belief, the Proxy Statement fails to disclose an offer made by JAMES HALPERIN in January, 1985, to acquire all the stock of BRIGGS for $3 a share.

g. On information and belief, the Proxy Statement fails to disclose the existence and value of legal claims of BRIGGS against the individually named defendants for repeated and long

standing diversions of corporate funds for their own personal use and benefit. In this regard, the Proxy Statement misstates that in 1984, EDWARD ROSENSTOCK, ROBERT ROSENSTOCK and GENSER received cash compensation of $78,000, $70,000 and $60,000, respectively. In 1984 their actual, and unreported, compensation vastly exceeded those amounts as it did in the years preceding 1984. BRIGGS has been used routinely by the individually named defendants as a personal cash box to defray tax-free the expenses incurred in pursuit of their opulent lifestyles. For example, BRIGGS cash generated in various ways from BRIGGS operations and/or corporate credit cards are and have been used to pay the expenses of EDWARD ROSENSTOCK incurred in maintaining two residences (New York and Florida), in commuting by air weekly between such residences, for dues and expenses for the Westview and Hillcrest Country Clubs (neither of which is used for business related purposes), both highly expensive golf clubs located in the State of Florida, and for his restaurant, limousine and clothing bills. BRIGGS cash and corporate credit cards are and have been used by ROBERT ROSENSTOCK, a bachelor, (i) to defray the expenses he has incurred and incurs in acquiring, maintaining and furnishing no less than two luxury residences in New York (apartments at 79th Street and Park Avenue, and a home in Great Neck, Long Island); (ii) to acquire and maintain membership in at least two expensive country clubs located in Florida (none of which is

used for business related reasons); (iii) to defray his extravagant travel, restaurant and entertainment expenses; (iv) to annually purchase in cash literally thousands of dollars of clothes made to his order by Fiorvanti Tailors of New York where the price of a custom made suite starts at approximately a modest $2,500. The exact amount of these tax-free diversions of BRIGGS monies for the six years prior to the commencement of this action is presently unknown to the plaintiffs, will be determined during the discovery process, and is now estimated to be approximately $750,000 per year.

h. On information and belief, the Proxy Statement fails to disclose and value the legal claims of BRIGGS based on the illegal and improper diversion of corporate opportunities by the individually named defendants, i.e., the acquisition by them of Ross Chevrolet Cadillac Oldsmobile, Inc. ("Ross") and Belgrave Oldsmobile, Inc. ("Belgrave"), both of which BRIGGS was in a position to acquire, and, with respect to Ross, the acquisition of which BRIGGS actually helped finance.

(i) On information and belief, in 1981 it was brought to the attention of the individually named defendants that Ross was available for acquisition at an extremely attractive price. Rather than present this attractive corporate opportunity to BRIGGS, which, had it been under a management not burdened by the conflicts of interest present here, would have been eager to

make the acquisition; EDWARD ROSENSTOCK and ROBERT ROSENSTOCK, acting out of a desire to personally benefit defendants themselves and in breach of their fiduciary duties to BRIGGS and its minority shareholders, arranged for the acquisition of Ross by ROBERT ROSENSTOCK personally using, in part, assets of BRIGGS to finance the acquisition. At the present time, ROBERT ROSENSTOCK and GENSER own all of its stock. Since the acquisition, the individually named defendants have caused BRIGGS to do business with Ross for their own personal financial benefit.

(ii) On information and belief, in 1983 it came to the attention of the individually named defendants that Belgrave was available for acquisition. Rather than present this attractive corporate opportunity to BRIGGS, which, had it been under the control of a management not burdened with the conflicts of interest present here, would have been eager to make the acquisition; the individually named defendants, for the personal financial benefit of defendants, ROBERT ROSENSTOCK and GENSER, and in breach of their fiduciary duties to BRIGGS and its minority shareholders, arranged for Belgrave to be acquired personally by ROBERT ROSENSTOCK and GENSER. In particular, that acquisition was not offered to BRIGGS because Belgrave was and is the owner of a large parcel of undervalued real estate

which the individually named defendants plan to develop for their own personal financial gain. Since that acquisition, Briggs has been caused by the individually named defendants to do business with Belgrave for the personal financial benefit of ROBERT ROSENSTOCK and GENSER. i. On information and belief, the Proxy Statement failed to disclose that during the period June 1984 through February 1985, the individually named defendants acquired BRIGGS stock in private transactions at prices in excess of $1.50.

j. The Proxy Statement failed to reveal that the Special Meeting of Shareholders of February 25, 1985, was invalidly called and could be of no legal effect. Section 605(a) of the New York Business Corporation Law (McKinney Supp. 1984) (the "BCL") mandates that a notice of a shareholders' meeting to approve a merger refer to and disclose the shareholders' statutory rights under the BCL's appraisal provisions. The Notice employed by the defendants to convene the meeting of February 25, 1985, contained no such reference or disclosure.

k. The Proxy Statement misrepresents that BRIGGS liquidation value is less than its going concern value when just the opposite is the case, in view of the actual market value of BRIGGS realty and the value of its unasserted claims against the individual defendants.

19. Defendants, by cashing out the minority shareholders at $1.50 per share, have placed a total value on BRIGGS' entire equity at less than $900,000. In no event, would the individual defendants sell their equity interest at $1.50 per share. Defendants, knowing that the fair market value of BRIGGS' total equity is greatly in excess of $900,000, are deliberately, and willfully deceiving and defrauding the minority stockholders of BRIGGS.

20. By virtue of the foregoing, equitable relief was, and is, available to the plaintiffs, individually and derivatively, under the exception stated in Sec. 623 Subd. (k) of the Business Corporation Law of New York and under its law applicable to breach of fiduciary duties.

21. The misrepresentations and omissions specified above would have been of actual significance in the deliberations of a reasonable disinterested director of Briggs and were, therefore, material. The likely ability to enjoin the merger under New York law supplies the causal link between the material misrepresentations and non-disclosures on the one-hand, and injury to Briggs and plaintiffs on the other; and, of course, said deception was in connection with the purchase or sale of securities. Hence, the freeze-out merger was in violation of Sec. 10(b) and Rule 10b-5.

COUNT II

22. Plaintiffs repeat and reallege the allegations contained in Paragraphs 2 through 30, as if fully set forth herein.

23. Defendants as controlling stockholders of BRIGGS and the individual defendants as directors of BRIGGS have breached their fiduciary duty to BRIGGS and to the minority stockholders of BRIGGS under New York State's common law and the exception to §623 subd. (k) of the BCL by forcing this deceptive and fraudulent merger upon the minority shareholders. Equitable relief, including rescission of the merger is appropriate, individually and derivatively.

COUNT III

24. Plaintiffs repeat and reallege the allegations contained in Paragraphs 2 through 21, and if fully set forth herein.

25. Defendants have violated New York General Business Law, Section 352-c, (the "Martin Act") by forcing this deceptive and fraudulent merger upon the minority stockholders.

COUNT IV

26. Plaintiffs repeat and reallege the allegations contained in paragraphs 2 through 21 as if fully set forth herein.

27. By virtue of the foregoing, the defendants have violated BCL §605(a) and the purported merger is therefore without effect and should be rescinded.

COUNT V

28. Plaintiffs repeat and reallege the allegations contained in Paragraphs 2 through 21, as if fully set forth herein.

29. The cause of action is also derivative on behalf of BRIGGS by reason of damages sustained by BRIGGS, caused by defendants' acts set forth in Paragraphs 18 (g) and (h).

30. Since the individual defendants, who have enriched themselves at the expense of BRIGGS and misappropriated BRIGGS' corporate opportunities, are all directors of BRIGGS, it would be futile to make a demand on those same directors to sue themselves on behalf of BRIGGS based on all the derivative claims in this Count.

31. Plaintiffs have no adequate remedy at law.

32. On May 20, 1985, plaintiffs herein commenced an action as Petitioners in the Supreme Court of the State of New York, County of Nassau, against BRIGGS LEASING CORPORATION, Respondent, to fix the fair value of Petitioners' shares as dissenting shareholders under §623 of the Business Corporation Law. Therein, Petitioners requested that prosecution of the appraisal proceeding be held in abeyance pending the final determination of this Federal action.

33. There is a related (individual) action filed in this Court entitled "ADRIENNE ROSENSTOCK HALPERIN, et. al., Plaintiffs, against ROBERT ROSENSTOCK, et. al., Defendants (Index No. 85 Civil 1258, Constantino, J.).

WHEREFORE, plaintiffs pray for an order and judgment:

I. That the action insofar as brought as a class action may be maintained as such.

II. That the merger aforesaid be set aside; or

III. That the terms of the aforesaid merger be reformed so that they are just, fair and equitable;

IV. That defendants account for the damages suffered by BRIGGS and the profits and benefits enjoyed by the individual defendants by reason of the wrongs set forth in Count V; and

V. That the Court give such other, further, and different relief as may be just, including damages, together with costs, disbursements and a reasonable fee for plaintiffs' attorneys.

Dated: July 1, 1985

LEVENTRITT LEWITTES & BENDER

By: /s/

A Member of the Firm
Attorneys for the Plaintiffs
1205 Franklin Avenue
Garden City, New York 11530
(516) 742-4250

APPENDIX G

GOODMAN-MARKS ASSOCIATES, INC.
REAL ESTATE APPRAISERS AND CONSULTANTS

Leventritt Lewittes & Bender
Page 2
June 13, 1997

In arriving at the appraised values, we have given consideration to all items influencing value. Included are the items of location, existing and projected competition, continued demand, current and anticipated market conditions, current mortgage rates, actual income, expenses and lease terms, government rules and regulations, income rates for similar properties, as well as the rates of return of competitive properties and investments.

As of February 26, 1985, the date of valuation, we estimate the market value of the subject property's fee owned land area to be:

TWO MILLION TWO HUNDRED SIXTY-FIVE THOUSAND DOLLARS ($2,265,000.00)

As of February 26, 1985, the date of valuation, we estimate the market value of the subject property's leasehold estate, subject to the existing ground lease, to be:

TWO HUNDRED SIXTY-FIVE THOUSAND DOLLARS
(265,000.00)

A report of 48 pages is attached hereto and made part hereof, and the valuation is expressly made subject to the conditions and comments appearing on such pages.

Very truly yours,

GOODMAN-MARKS ASSOCIATES, INC.

/s/	/s/
Bernard Goodman, MAI, CRE President Certified General Real Estate Appraiser New York Certificate #460690	Anthony C. Iaccio, MAI Senior Vice President Certified General Real Estate Appraiser New York Certificate #464645

APPENDIX H

PAINE WEBBER JACKSON & CURTIS
Incorporated

Established 1879
Members New York Stock Exchange, Inc. and other
Principal Exchanges
25 Broad Street
New York, New York 10004
(212) 437-2121

March 25, 1985

BY HAND

Briggs Leasing Corporation
777 Northern Blvd.
Great Neck, New York 11022

Gentlemen:

As the registered holder of 7476 common shares of Briggs Leasing Corporation, Pursuant to Section 523(f) of the New York Business Corporation Law, we are hereby submitting the following certificates:

We are submitting these certificates for notation of election to dissent with the understanding that we, as registered holders of the shares, as well as the individual beneficial

shareholders, namely Morgan H. Grace (1400 shares), Oliver R. Grace (4000 shares), John E. Grace trust (2 shares), and Lorraine Grace (2074) shares), are not waiving any rights as shareholders objecting to the merger, in law or equity, including without limitation, the right to assert a claim for rescission based on a breach of fiduciary obligation, fraud, violations of New York's Martin Act and Securities Act of 1934.

The right to assert the above claims is based on majority stockholder's unlawful forced purchase of the minority shareholders' stock at a grossly inadequate price in this self-deal merger, whereby the majority shareholders exercised their power to force in unconscionable transaction upon the helpless minority. It is also noteworthy that an aggregate of 141,441 shares of common stock out of a total minority interest of 163,901 shares or 86 percent of the minority dissented from this fraudulent transaction.

Very truly yours,

/s/

Mark C. Clyne
Ass't Vice President
Proxy Department

MCC/df

PLAINTIFF'S EXHIBIT NO. 28